95-1251

No. _____

Supreme Court, U.S.
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In The

Supreme Court of the United States

October Term, 1995

THOMAS A. WARMUS,

Petitioner,

v.

LEWIS E. MELAHN, JAMES OETTING and WILLIAM HOBBS, III,

Respondents.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Eighth Circuit

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QUESTIONS PRESENTED FOR REVIEW

1. Based upon the *Younger* abstention, should the United States District Court dismiss with prejudice a case filed pursuant to 42 U.S.C. 1983 which solely sought monetary damages?

2. In order for the federal courts to dismiss a case with prejudice based upon the *Younger* abstention, must the interference with the state court proceeding be substantial?

3. In a case seeking solely monetary damages in which the Petitioner, Plaintiff, had no opportunity to raise the constitutional issues in the state court proceedings, did the Court err in dismissing the federal action with prejudice instead of staying the case pending resolution of the state court action?

LIST OF POTENTIAL PARTIES TO THE PROCEEDINGS

A list of all parties to the proceedings in both the United States District Court as well as the United States Court of Appeals For The Eighth Circuit, appear in the caption of the case.

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REFERENCE TO OFFICIAL AND UNOFFICIAL REPORTS OF OPINIONS DELIVERED IN THE CASE BY OTHER COURTS OR OTHER ADMINISTRATIVE AGENCIES

1. Order of United States District Court For The Western District of Missouri, Central Division, entered November 29, 1993 dismissing Plaintiff's Complaint with prejudice based upon *Younger* abstention.

2. Order of United States Court of Appeals For The Eighth Circuit entered August 8, 1995 affirming decision of the United States District Court For The Western District of Missouri.

3. Order of United States Court of Appeals For The Eighth Circuit entered September 21, 1995 denying Suggestions For Rehearing En Banc and denying Petition For Rehearing by the panel.

GROUNDS OF JURISDICTION

The Order sought to be reviewed is an opinion of the United States Court of Appeals for the Eighth Circuit entered August 8, 1995.

On September 21, 1995, the United States Court of Appeals for the Eighth Circuit entered its Order denying the Suggestions For Rehearing En Banc and also denying the Petition For Rehearing By The Panel.

Jurisdiction of this Court is conferred on the United States Supreme Court pursuant to 28 U.S.C. § 1254 because this is an application for Writ of Certiorari, after

a rendition of a judgment or decree in the United States Court of Appeals.

STATEMENT OF THE CASE

Petitioner, Thomas Warmus ("WARMUS") is the ultimate beneficial owner of American Financial Security Life Insurance Company ("AFSLIC"), a Missouri domestic insurance company. WARMUS had been in the insurance industry for over 35 years and during that time, developed relationships with numerous insurance accounts or agencies, which constituted a valuable and profitable "book of business" owned by WARMUS. WARMUS filed suit in the United States District Court For The Western District of Missouri seeking solely monetary damages against Respondents Lewis Melahn ("MELAHN"), former Director of Insurance of the Missouri Department of Insurance ("MDI"); James Oetting ("OETTING"), former Chief Financial Examiner of MDI; and William Hobbs ("HOBBS"), an agent or representative of MDI, alleging that these Defendants together with others at MDI and the Michigan Insurance Bureau in violation of 14 U.S.C. § 1983 and without due process of law, conspired to: (1) deprive WARMUS of his rights to properties including AFSLIC; (2) drive WARMUS out of the insurance industry; (3) destroy WARMUS's valuable and profitable book of business; and (4) destroy WARMUS's excellent reputation in the industry.

In his federal complaint, WARMUS did not contest the constitutionality of Missouri insurance laws, nor did he contest the validity of the order placing AFSLIC into

rehabilitation, but rather alleged that the personal actions of Respondents, MELAHN, OETTING and HOBBS, under color of law violated WARMUS's civil rights.

Jurisdiction of the federal court was invoked pursuant to 28 U.S.C. § 1331 and 28 U.S.C. § 1343. (See App. pgs. 58-86)

On November 29, 1994, on a Motion To Dismiss filed pursuant to Rule 12 (b), Federal Rules of Civil Procedure, the United States District Court dismissed Plaintiff's initial Complaint with prejudice on the basis of the *Younger* abstention. (See App. pgs. 11-16)

The pending state court proceedings on which the District Court based its dismissal was the rehabilitation of AFSLIC pending in the Missouri State Circuit Court and an appeal to the State Appellate Court of the order of the Missouri State Circuit Court placing AFSLIC into rehabilitation. The decision of the Missouri State Circuit Court placing AFSLIC into rehabilitation was affirmed by the Appellate Court for the Western District of Missouri during the pendency of the appeal of the United States District Court's decision in the instant case. See *Melahn v. American Financial Security Life Insurance Company*, 869 SW 2d 90 (Mo. App. 1993)

WARMUS was never a party to the state court rehabilitation proceedings of AFSLIC. Those proceedings were tried before a Special Master on an eight count complaint. AFSLIC prevailed on five of the eight counts with both the Special Master and the Court finding that equitable estoppel existed against MDI because of the conduct of MDI, including the three Defendants in the instant case. (See App. pgs. 17-56) Notwithstanding the

finding of estoppel, the State Circuit Court affirmed MDI's decision to place AFSLIC into rehabilitation due to a disallowance of three months of reinsurance credits on a reinsurance treaty, which disallowance rendered AFSLIC statutorily insolvent for a limited period of time.

In its Complaint in the United States District Court, WARMUS contested neither the rulings nor factual findings of the Missouri State Circuit Court, but sued the Defendants/Respondents for monetary damages.

On August 8, 1995, the United States Court of Appeals For The Eighth Judicial Circuit affirmed the ruling of the United States District Court stating:

> "Secondly, we believe by Appellees personal conduct may become an issue in AFSLIC's rehabilitation. For example, were Warmus to win his federal damage action prior to the conclusion of AFSLIC's rehabilitation, the resulting federal judgment would amount to a declaration that Appellees, all of whom are high ranking officials at MDI, conspired to drive Warmus out of business without due process of the law . . . Such an effective declaration in our view might well have the practical effect of undermining the validity and integrity of the State – court rehabilitation proceeding."

On September 21, 1995 the United States Court of Appeals for the Eighth Circuit denied both the Petition For Rehearing and Petition For Rehearing En Banc.

ARGUMENT

POINT I

YOUNGER INAPPROPRIATE WHEN ONLY RELIEF REQUESTED WAS MONETARY DAMAGES

This Court in *Deakins v. Monaghan,* 484 U.S. 193 (1988), declined to decide whether the *Younger* doctrine applies to a federal case seeking only monetary relief stating at page 102: "We need not decide the extent to which Younger doctrine applies to a federal action seeking only monetary relief . . . "

WARMUS respectfully requests that this Honorable Court now consider whether the *Younger* doctrine apply in a case seeking solely monetary damages. This is an important question of federal law which has not been, but should be settled by this Court.

While it is recognized and acknowledged that the regulation of insurance is a matter which has been left to the States, (See *McCarran Ferguson Act, 15 U.S.C. § 1012 et seq.)* the right to regulate does not give the officials or representatives of States' Departments of Insurance the right to violate an individual's constitutional right under *color of law,* without that individual being able to seek redress for violation of his rights in the federal courts. Unfortunately, the decision in the case *sub judice* permits such a state of affairs to exist. The decision of the Court of Appeals in the instant case has far reaching implications not only in the insurance industry, but in all regulated industries. If the decision of the Eighth Circuit Court of Appeals is allowed to stand in the instant case, a clear message is sent that individuals or entities operating within a regulated industry, profession or any form of

license, cannot look toward the federal courts to obtain redress for a violation of their constitutional rights.

Younger abstention was based on the fundamental policy against interference with state criminal prosecution. *Younger v. Harris,* 401 U.S. 37 (1983). *Younger* abstention has been extended to cases other than criminal cases to include administrative as well as civil cases. See *Huffman v. Pursue Limited,* 420 U.S. 592 (1975) and *Pennzoil Company v. Texaco, Inc.,* 481 U.S. 1 (1987).

In all of these cases involving the *Younger* abstention, the Plaintiff in the federal court case sought some interference with the state court proceedings. In the instant case, WARMUS seeks only monetary damages against three individuals based on their personal actions, and seeks no interference with the State Rehabilitation proceedings.

Even though the applicability of *Younger* abstention has been extended beyond criminal cases, no court has departed from the doctrine that abstention should be the exception and not the rule and only appropriate when absolutely necessary to protect against interference with important state interest. In *Deakins v. Monaghan,* 484 U.S. 193 at 203 (1988) this Court stated:

> This court repeatedly has stated that the federal courts have a "virtually unflagging obligation" to exercise their jurisdiction except in those extraordinary circumstances " 'where the order to the parties to repair to the state court would clearly serve an important countervailing interest' " *Colorado River Water Conservation Dist. v.*

United States, 424 U.S. 800, 813, 817 (1976) quoting *County of Allegheny v. Frank Mashuda Co.*, 360 U.S. 185, 188-189 (1959);

In a case in which one is seeking only monetary damages, especially against three individuals, there can be no potential interference with state proceedings. The rationale for the *Younger* abstention vanishes in a suit in which monetary damages is the only relief sought.

POINT II

SUBSTANTIAL INTERFERENCE WITH STATE PROCEEDINGS SHOULD BE NECESSARY TO JUSTIFY THE YOUNGER ABSTENTION

The Eighth Circuit Court of Appeals found that WARMUS's civil rights complaint would interfere with the state court proceedings in two possible ways. The first was the finding that the conduct of MDI was an issue in the State Court appeal with the United States Appellate Court stating "First, Appellees' conduct was clearly an issue in Appellant's appeal in as much as AFSLIC argued that MDI should be equitably estopped from disallowing the full nine months of Lloyds treaty reserve credits". The second basis was that the Court of Appeals held that a finding in WARMUS's favor in the federal case could cause embarrassment to the MDI in the rehabilitation proceedings stating:

> "Secondly, we believe Appellees personal conduct may become an issue in AFSLIC's rehabilitation. For instance, were WARMUS to win his federal damages actions prior to the conclusion of AFSLIC's rehabilitation, the resulting federal judgment would amount to declaration

> that Appellees, all of whom are high ranking officials at MDI, conspired to drive WARMUS out of business without due process . . . Such an effective declaration in our view might well have the practical affect of undermining the validity and integrity of the state-court rehabilitation proceedings."

The commonality of a single issue in a state appellate case and the federal civil rights case, and the fact that a declaration in the federal civil rights case could be critical of the personal actions of three high ranking individuals at MDI is not the type of "important countervailing interest" which the United States Supreme Court found essential to justify a departure from the federal court's "virtually unflagging obligation" to exercise their jurisdiction in every case in which the United States Supreme Court considered the *Younger* abstention, from *Younger v. Harris*, 401 U.S. 37 (1970) through the present.

WARMUS respectfully suggests that the prosecution of his federal civil rights case would have no interference with the state court appeal (which has since been concluded) nor with the State Court Rehabilitation proceedings. The Special Master and the State Rehabilitation Court had already rendered their decision prior to WARMUS's federal action being filed.

The issues in the State Court case and the ensuing appeal, and the federal case were completely different. In the State Court Rehabilitation trial, both the Special Master and the State Court made certain factual findings regarding the actions of officials, employees and representatives of MDI. Both the Special Master and the Court ruled that based upon those factual findings, MDI was

equitably estopped from changing the accounting methodology relative to a reinsurance treaty.[1]

During the State Court appeal, WARMUS never challenged the factual findings of the Special Master nor the trial court, since both found that MDI's conduct warranted the extraordinary finding of estoppel against a state agency. Rather, AFSLIC in its state court appeal challenged the manner that estoppel was to be applied; namely, in addition to the accounting methodology, AFSLIC argued estoppel should also be applied to the effective dates or coverage period of the reinsurance treaty.

The appeal in the State Rehabilitation case was concerned whether statutory grounds existed to place AFSLIC into rehabilitation and whether the decision to place AFSLIC into rehabilitation was an abuse of MDI's discretion. The federal civil rights case did not challenge the appropriateness of the order of rehabilitation or the application of the *doctrine of estoppel*, but rather addressed the personal conduct of individuals. Thus, even if the appeal in the State Rehabilitation case was not decided during the pendency of the appeal in the federal case, there could be no possible interference between the federal case and the state appeal, as the issues were completely different.

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[1] The accounting methodology was the method for determining the amount of credits that a company was entitled to take on its financial statements for reinsurance, which it ceded to another carrier.

Moreover, while it is clear that a finding by the U.S. District Court that Defendants conspired to drive WARMUS out of business without due process of law might cause embarrassment to MDI, such a finding would not interfere with the rehabilitation proceedings. In fact, prior to the federal case being filed, the State Rehabilitation Court found that the conduct of MDI was so outrageous as to justify the extraordinary findings of estoppel. While that should have caused embarrassment to MDI, it did not interfere with the state court rehabilitation proceedings. The state court proceedings concerned whether the further operation of AFSLIC was financially hazardous to its policyholders, creditors or the public, or whether AFSLIC violated some other statutory ground which justified rehabilitation pursuant to § 375.1165 R.S.Mo. The State Court proceedings was not designed to protect the reputation or integrity of officials at the Division of Insurance.

In *Younger v. Harris*, 401 U.S. 37 (1970), the plaintiff who was indicted in state court attempted to enjoin the prosecution of the state court case. In *Middlesex County Ethics Committee v. Garden State Bar Association*, 457 U.S. 424 (1982), the Plaintiff attempted to enjoin actions of the state bar. In *New Orleans Public Service Inc. v. Council of the City of New Orleans*, 491 U.S. 350 (1989) the plaintiff attempted to enjoin actions of an agency. In *Pennzoil Company v. Texaco, Inc.*, 481 U.S. 1 (1987) the Plaintiff attempted to enjoin collection efforts on a state court judgment. In *Alleghany v. McCartney*, 896 F.2d 1138 (8th Cir. 1990), the Plaintiff sought to enjoin actions of the Director of Insurance. In *Deakins v. Monaghan*, 484 U.S. 193 (1988), the Plaintiff sought return of documents

seized pursuant to a warrant as well as compensatory and punitive damage.

In *Middlesex County Ethics Committee v. Garden State Bar Association*, 457 U.S. 424 at 432 (1982), this Court discussed the type of important state interests necessary to justify the extraordinary ruling of abstention stating:

> The policies underlying *Younger* are fully applicable to noncriminal judicial proceedings when important state interests are involved. *Moore v. Sims*, 442 U.S. 415, 423, 99 S.Ct. 2371, 2377, 60 L.Ed.2d 994 (1979); *Huffman v. Pursue, Ltd.*, 420 U.S. 592, 604-605, 95 S.Ct. 1200, 1208, 43 L.Ed.2d 482 (1975). The importance of the state interest may be demonstrated by the fact that the noncriminal proceedings bear a close relationship to proceedings criminal in nature, as in *Huffman, supra*. Proceedings necessary for the vindication of important state policies or for the functioning of the state judicial system also evidence the state's substantial interest in the litigation. *Trainor v. Hernandez*, 431 U.S. 434, 97 S.Ct. 1911, 52 L.Ed.2d 486 (1977); *Juidice v. Vail*, 430 U.S. 327, 97 S.Ct. 1211, 51 L.Ed.2d 376 (1977). Where vital state interests are involved, a federal court should abstain "unless state law clearly bars the interposition of the constitutional claims". *Moore*, 442 U.S., at 426, 99 S.Ct., at 2379.

The common thread in all of the above cases was a substantial interference with an ongoing state proceedings, not an indirect affect, such as potential embarrassment or that an issue might be similar in both the state and federal proceedings. The interference with the State Court proceedings in the instant case is non-existent, or if existent, insignificant. WARMUS should not be deprived

of his right to seek relief in a federal forum for violation of his federal constitutional rights based upon the possibility of interference.

POINT III

COURT OF APPEALS ERRED IN DISMISSING THE FEDERAL COURT ACTION WITH PREJUDICE RATHER THAN STAYING THE CASE

The decision of the United States District Court which was affirmed by the United States Court of Appeals For The Eighth Circuit in dismissing this case with prejudice instead of staying the action was contrary to the law as set forth by the United States Supreme Court.

In *Deakins v. Monaghan*, 484 U.S. 193 at 202 (1988) this Court stated,

> "We need not decide the extent to which *Younger* doctrine applies to a federal action seeking monetary relief, however, because even if the *Younger* doctrine requires abstention here, the District Court has no discretion to dismiss rather than to stay claims for monetary relief they cannot be redressed in the state court proceedings."

The State Court proceedings involving the rehabilitation of AFSLIC was a statutory proceedings seeking rehabilitation of an insurance company under § 375.1165 R.S.Mo. and governed exclusively by the Missouri Insurance Code. *O'Malley v. Prudential Casualty & Surety Company*, 80 SW 2d 896 (Mo. 1935), *State ex rel. ISC Financial Corporation v. Kinder*, 684 SW 2d 910 (Mo. App. 1985),

Melahn v. Continental Security Life Insurance Company, 793 SW 2d 425 (Mo.App. 1990).

Section 375.1165 R.S.Mo. does not provide any right or opportunity for an insurance company or its officers, directors or stockholders to file a suit for damages in a rehabilitation proceedings. Furthermore, no other provision of the Missouri Insurance Code provides for such relief. Therefore, the only opportunity that WARMUS or any company of which he was a principal, officer or director including AFSLIC had to file suit, was when WARMUS brought the proceedings in the United States District Court.

The United States Circuit Court of Appeals erroneously concluded that since the directors of AFSLIC which included WARMUS, filed a motion in the State Rehabilitation case for authority to file an independent civil rights suit on behalf of AFSLIC against Defendants/Respondents; and since the State Court denied such a request, that WARMUS had the opportunity to raise the constitutional issue in the State court proceedings.[2]

To the contrary, if AFSLIC had the right to file a civil rights action in the state rehabilitation proceedings, the Directors of AFSLIC would have not needed to ask the State Court to delegate to them authority to file such an independent civil rights suit on behalf of AFSLIC, AFSLIC could have simply filed suit. Since the state court

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[2] The Motion filed by the Directors of AFSLIC seeking authority to file suit on behalf of AFSLIC was filed after the trial in State Court and after an Order of Rehabilitation had been entered.

denied the request to delegate authority, WARMUS filed suit in federal court for violation of his own civil rights; however, was unable to file suit on behalf of AFSLIC for the violation of AFSLIC's civil rights.

Pursuant to § 375.1166 R.S.Mo., the recording of the Rehabilitation Order "vest title to all assets of the insurer in the rehabilitator". After the Order of Rehabilitation all assets of AFSLIC including the cause of action to file a civil rights action statutorily vests in the rehabilitator, which pursuant to § 375.1166(1) R.S.Mo. is the director of insurance. Therefore, filing a civil rights suit on behalf of AFSLIC, required the consent of the rehabilitator. Section 375.1168.2 R.S.Mo. states with regard to the rehabilitator "he shall have all the powers of the directors, officers, and managers, whose authority shall be suspended, except as they are redelegated by the rehabilitator".

The critical issue in the motion to delegate authority filed in the State Rehabilitation Court was whether the State Rehabilitation Court had jurisdiction to grant such a request, with AFSLIC stating in its Suggestions In Support of its Motion:

> The issue is whether the Circuit Court of Cole County, Missouri, which is vested under § 375.1166 RSMo., with statutory authority to supervise the rehabilitation, possesses implied or inherent authority to empower the directors or officers of AMERICAN FINANCIAL to initiate a legal suit on behalf of AMERICAN FINANCIAL to bring the assets of the company's claim against MELAHN, HOBBS and OETTING into the estate in rehabilitation.

MDI recognized that the motion was requesting that the state court delegate to AFSLIC's directors and officers the authority to file suit on behalf of AFSLIC, stating in their Suggestions In Opposition To The Motion:

> Now these former officers and directors of AFSLIC have taken the incredible step of filing a motion requesting the Court to force the Director of the Department of Insurance to delegate his statutory authority to them so they may sue former and present employees and agents of the Missouri Department of Insurance.

MDI then argued that the State Rehabilitation Court could not force the director to delegate the authority to file suit, stating:

> The Director is statutorily vested with the authority to defend and conduct litigation on behalf of an insurance company in rehabilitation. *The court cannot order the Director to delegate those duties imposed upon him by statute. (emphasis added)*

The State Circuit Court in Jefferson City, Missouri denied the Motion For Authority To File Suit by docket entry without explanation, presumably because the court found it had no jurisdiction to enter such an Order. Thus, instead of the suit in the United States District Court being filed by WARMUS and AFSLIC, WARMUS became the sole Plaintiff seeking only those damages which he individually sustained. WARMUS could not have raised AFSLIC's or his constitutional claims in the State Rehabilitation Court. The dismissal with prejudice of

WARMUS's civil rights claim, left WARMUS without any forum to seek redress of his constitutional rights.

CONCLUSION

The decision of the Court of Appeals For The Eighth Circuit extends the *Younger* abstention to areas in which the interference with the State Court proceedings is non-existent or insubstantial. It effectively eliminates the federal courts as a viable remedy for those people involved in regulated industries who claim a violation of their constitutional rights. It leaves WARMUS who has been deprived of his constitutional rights under *color of law* by Respondents, MELAHN, OETTING, and HOBBS, without any viable remedy. Petitioner, WARMUS, respectfully requests that this Honorable Court grant certiorari and proceed to determine the case on the merits.

Respectfully submitted,

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APPENDIX

APPENDIX

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UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 93-4083

Thomas A. Warmus, Appellant, v. Lewis Melahn; James Oetting; William Hobbs, Appellees.	*	Appeal from the United States District Court for the Western District of Missouri.

Submitted: September 13, 1994

Filed: August 8, 1995

Before HANSEN, Circuit Judge, FLOYD R. GIBSON and HENLEY, Senior Circuit Judges.

HENLEY, Senior Circuit Judge.

Thomas A. Warmus appeals from a judgment of the district court dismissing with prejudice his 42 U.S.C. § 1983 damages action against Lewis Melahn, the former director of the Missouri Department of Insurance (MDI), and two of his subordinates, James Oetting and William Hobbs. In dismissing the court acted under the *Younger* abstention doctrine, which is premised on the "long-standing public policy against federal court interference

with state court proceedings." *Younger v. Harris*, 401 U.S. 37, 43 (1971). We affirm.

BACKGROUND

Warmus is the owner of American Way Holding, Inc., a holding company comprised of seven insurance companies, including American Way Life Insurance Company (Life), and three non-insurance companies. Prior to 1989, Warmus had been feuding with the Michigan Insurance Bureau over some of the credit-life business generated by Life. Consequently, in May 1989 Warmus directed American Way Holding to purchase American Financial Security Life Insurance Company (AFSLIC), a Missouri-domiciled premium credit-life and disability insurance company. To avoid further conflict with the Michigan bureau, Warmus ordered that Life's entire block of credit-life business be transferred from Life to AFSLIC, which is regulated by MDI. By early 1992, this transfer of business was complete.

In March 1992, due to the company's excessive premiums-to-surplus ratio, Melahn, as director of MDI, ordered AFSLIC into administrative supervision. *See* Mo. Rev. Stat. § 375.1160.2 (1) (a-e) (1991). Soon thereafter, AFSLIC attempted to right itself financially by entering into a series of reinsurance treaties. In June 1992, it entered into one such treaty with Lloyds of London (the "Lloyds treaty"). The Lloyds treaty was to be in force during the last three quarters of 1992, and, according to projections, was to increase AFSLIC's reserves by some $8,000,000. This increase in reserves, it was hoped, would

improve the company's premiums-to-surplus ratio to an acceptable regulatory level.

However, before the Lloyds treaty could be finalized, Hobbs, the Melahn-appointed administrative supervisor of AFSLIC, had to approve it. Although Hobbs had some questions about the methodology AFSLIC used to account for the treaty's reserve impact, he eventually approved it in early August 1992. Later, Hobbs's superiors at MDI, Oetting and Melahn, also approved the Lloyds treaty.

In October 1992, a dispute with MDI arose over a different reinsurance treaty – one AFSLIC had executed with American Trend Life Insurance Company (the "Trend treaty"). MDI contended the Trend treaty was invalid because American Trend was not an authorized Missouri reinsurer. AFSLIC bowed to this contention and restated its September 30, 1992 financial statement to reflect the elimination of all Trend reserve credits.

The elimination of Trend reserve credits, however, caused a reserve-credit void for the first three quarters of 1992. To remedy this problem, AFSLIC chose to reapply the Lloyds treaty, which, by its terms, was in force during the last three quarters of 1992 to the first three quarters of 1992. In other words, AFSLIC substituted the Lloyds treaty for the Trend treaty. This substitution of reinsurance treaties filled AFSLIC's reserve-credit void for the first three quarters of 1992, and allowed it to report a positive surplus-capital balance for the three quarters ending September 30, 1992.

In December 1992, MDI conducted an examination of AFSLIC. In its examination report, in a seeming reversal

from the prior positions of Hobbs, Oetting and Melahn, MDI revealed that it now disapproved of the methodology AFSLIC was using to account for the reserve impact of the Lloyds treaty. Using what it perceived to be the proper accounting methodology, MDI calculated the Lloyds treaty – at the time being used as a substitute for the Trend treaty – to have spawned only a fraction of the reserve credits taken by AFSLIC in its September 30, 1992 financial statement. By MDI's accounting, AFSLIC was actually insolvent as of September 30, 1992.

In light of the company's apparent insolvency, on February 1, 1993 MDI filed a petition for rehabilitation against AFSLIC in the Circuit Court of Cole County. *See* Mo. Rev. Stat. § 375.1165 (1991). The circuit judge referred the matter to a special master. The master found that MDI should be estopped from alleging AFSLIC insolvent on the basis of faulty accounting procedures. However, the master nonetheless concluded that AFSLIC was insolvent as of September 30, 1992 because the company had illegally substituted the Lloyds treaty for the Trend treaty. Although the circuit court apparently disagreed with the master's conclusion that MDI should be estopped from challenging AFSLIC's accounting methods, it agreed that AFSLIC was insolvent and ordered it into rehabilitation. In April 1993, AFSLIC appealed the rehabilitation order to the Missouri Court of Appeals.

In May 1993, at the behest of Warmus, AFSLIC filed a "Motion for Authority to File Suit on Behalf of Defendants" in the Circuit Court of Cole County. In that motion, AFSLIC sought authority to file a section 1983 damages action against appellees. The motion was denied, and AFSLIC did not appeal the denial.

While AFSLIC's appeal of the rehabilitation order was pending, in June 1993, as "beneficial owner, president and director" of AFSLIC, Warmus filed this section 1983 action in the district court against appellees in each's personal capacity. Seeking money damages only, Warmus challenged appellees' conduct during AFSLIC's administrative supervision. Among other things, Warmus alleged that while AFSLIC was in administrative supervision, appellees, acting in violation of his federal constitutional rights, conspired with the Michigan Insurance Bureau to drive AFSLIC out of business.

Appellees subsequently moved to dismiss on the basis of *Younger* abstention. Applying the three factors set forth in *Middlesex County Ethics Comm. v. Garden State Bar Ass'n*, 457 U.S. 423, 432 (1982), the district court agreed that *Younger* abstention was warranted and dismissed Warmus's civil rights action with prejudice. The court found that 1) AFSLIC's appeal was an ongoing state proceeding, *see New Orleans Public Serv., Inc. v. Council of the City of New Orleans*, 491 U.S. 350, 369 (1989) ("for *Younger* purposes, the State's trial-and-appeals process is treated as a unitary system"); 2) the appeal implicated the important state interest of regulating insurance companies; and 3) Warmus had an adequate opportunity to raise his constitutional claims in the appeal. Warmus now appeals the district court's *Younger* dismissal.

DISCUSSION

I.

We begin with basic *Younger* principles. The *Younger* abstention doctrine is grounded both in federalism and

comity, which dictates that " '[t]he National government, anxious though it may be to vindicate and protect federal rights and interests, always endeavors to do so in ways that will not unduly interfere with the legitimate activities of the States.' " *Allegheny Corp. v. McCartney*, 896 F.2d 1138, 1142 (8th Cir. 1990) (quoting *Younger*, 401 U.S. at 44). Thus, when a federal action is projected to unduly interfere with ongoing state proceedings "so important that exercise of federal judicial power would disregard the comity between the states and federal government," federal courts have the discretion to abstain. *Pennzoil v. Texaco, Inc.*, 481 U.S. 1, 11 (1987); *see Yamaha Motor Corp. v. Riney*, 21 F.3d 793, 798 (8th Cir. 1994) (district court's decision to abstain under *Younger* reviewed for an abuse of discretion).

From these basic principles, it becomes clear that some measure of potential undue federal interference is a *Younger* prerequisite. *See Davis v. Lansing*, 851 F.2d 72, 77 (2d Cir. 1988) ("*Younger* itself speaks of interference with state proceedings"). "In the typical *Younger* case, [where] the federal plaintiff is a defendant in ongoing or threatened state court proceedings seeking to enjoin continuation of those state proceedings," *Crawley v. Hamilton County Comm'rs*, 744 F.2d 28, 30 (6th Cir. 1984), the source of such interference – the federal injunction – is obvious. Likewise, the source is obvious where the federal plaintiff seeks declaratory relief designed to adjudicate issues identical to those raised in ongoing state proceedings. *See Samuels v. Mackell*, 401 U.S. 66, 72 (1971) (in such case "the declaratory relief alone has virtually the same practical impact as a formal injunction would"); *see also Rogers v. Desidiero*, No. 95-1228, 1995 WL 366203 at *1 (7th Cir. June

20, 1995) ("abstention under Younger's designed to prevent interference with proceedings presenting important issues of state policy or power either direct (as by enjoining their continuation) or indirect (as by deciding an issue before the state tribunal and, under the law of preclusion, preempting the State's consideration of the issue)").

In challenging the district court's decision to invoke *Younger* abstention in this case, Warmus seizes upon what he perceives to be an absence of potential undue federal interference. He maintains that his federal action, since it seeks money damages only and neither injunctive nor declaratory relief, did not interfere with AFSLIC's appeal of the rehabilitation order and will not interfere with AFSLIC's rehabilitation currently pending in the Circuit Court of Cole County, *i.e.*, the two ongoing state proceedings.

The Supreme Court has not decided the question whether *Younger* is applicable to a federal action like Warmus's "seeking only monetary relief." *Deakins v. Monaghan*, 484 U.S. 193, 202 (1988); *Juidice v. Vail*, 430 U.S. 327, 339 n.16 (1976) ("we intimate no opinion as to the applicability of [*Younger*] principles to a § 1983 suit seeking only [damages] in the district court"). We, however, have recognized that a federal money damages action can, in some circumstances, interfere with ongoing state proceedings sufficiently to warrant abstention. *See Wolfson v. Mutual Benefit Life Ins. Co.*, 51 F.3d 141, 147 (8th Cir. 1995) ("we do not read the Supreme Court's abstention jurisprudence as completely foreclosing abstention in money damages cases"); *see also McCurry v. Allen*, 606 F.2d 795, 799 (8th Cir. 1979) (applying *Younger* abstention doctrine

in section 1983 action seeking money damages only), *rev'd on other grounds*, 449 U.S. 90 (1980). Such interference is possible, however, if only the issues presented in the federal damages action have a "substantial relationship to . . . [the ongoing] state proceeding." *See Lannan v. Maul*, 979 F.2d 627, 631 (8th Cir. 1992); *Gywnedd Properties, Inc. v. Lower Gwynedd Township*, 970 F.2d 1195, 1201 (3d Cir. 1992) ("where abstention is appropriate, there is often a nexus between the claims asserted in the federal action and the defenses or claims asserted or available in the state action"); *AFCME v. Tristano*, 898 F.2d 1302, 1305 (7th Cir. 1990) (*Younger* abstention unwarranted because "the issues in the federal suit are substantially different from the issues in the state proceedings").

Acknowledging our *Lannan* "substantial relationship" test, or something close to it, Warmus contends that the issues comprising his federal damages claim are not substantially related to either of the two ongoing state proceedings. He observes that his damages action only challenges the personal conduct of three Missouri insurance officials which occurred during AFSLIC's administrative supervision. In contrast, he asserts AFSLIC's appeal strictly "concerns whether AFSLIC was operating in a hazardous condition as of September 30, 1992 and whether rehabilitation was warranted." Likewise, AFSLIC's rehabilitation, he further asserts, merely concerns "the condition or status of an insurance company in rehabilitation."

We agree with Warmus that his federal damages action is generally confined to challenging appellees' personal conduct. We disagree, however, with the notion that

appellees' personal conduct bears no substantial relationship to either of the ongoing state proceedings. First, appellees' conduct was clearly in issue in AFSLIC's appeal inasmuch as AFSLIC argued that MDI should be equitably estopped from disallowing the full nine months of Lloyds treaty reserve credits. *See Angoff*, 869 S.W.2d at 92. Although it is unclear who at MDI made the decision to disallow the full number of credits, appellees were the ones at MDI who originally approved the Lloyds treaty. In that way, they created the basis for AFSLIC's equitable estoppel argument directed at MDI. Secondly, we believe appellees' personal conduct may become an issue in AFSLIC's rehabilitation. For instance, were Warmus to win his federal damages action prior to the conclusion of AFSLIC's rehabilitation, the resulting federal judgment would amount to a declaration that appellees, all of whom are high-ranking officials at MDI, conspired to drive Warmus out of business without due process of law. *See Fair Assessment in Real Estate Ass'n v. McNary*, 454 U.S. 100, 113 (1981) ("[p]etitioners will not recover damages under § 1983 unless a district court first" declares their constitutional rights were violated). Such an effective declaration, in our view, might well have the practical effect of undermining the validity and integrity of the state-court rehabilitation proceedings. *See Samuels*, 401 U.S. at 72 (suggesting that courts contemplating *Younger* abstention focus on the "practical effect" of the requested federal relief).

Warmus's federal damages action therefore bears a substantial relationship to AFSLIC's appeal of the rehabilitation order, as well as to its rehabilitation currently pending in state circuit court. *See Lannan*, 979 F.2d at 631.

Furthermore, given this substantial relationship to both proceedings, it follows that the vital prerequisite to *Younger* abstention – potential undue federal interference – is present in this case. Thus, provided the three *Middlesex* factors can be satisfied, the district court acted within its discretion in abstaining under *Younger*. Predictably, Warmus contends none of the three *Middlesex* factors can be satisfied. We address each in turn.

Regarding the first *Middlesex* factor, Warmus argues that since he was not a party to either AFSLIC's appeal or its rehabilitation, no ongoing state proceedings existed with respect to him at the time he filed his federal complaint. *See Middlesex*, 457 U.S. at 432. We disagree. Since Warmus is the "beneficial owner, officer, and director" of AFSLIC, he is subject to *Younger* considerations otherwise applicable only to AFSLIC. *See Doran v. Salem Inn*, 422 U.S. 922, 928 (1975) ("there plainly may be some circumstances in which legally distinct parties are so closely related that they should all be subject to the *Younger* considerations which govern any one of them"); *see also Postscript Enters., Inc. v. Peach*, 878 F.2d 1114, 1116 (8th Cir. 1989); *Women's Serv., P.C. v. Douglas*, 653 F.2d 355, 358 (8th Cir. 1981).

Warmus cannot, and does not, seriously dispute that the second *Middlesex* factor can be satisfied. Both AFSLIC's appeal and its rehabilitation involved the subject matter of insurance regulation. We have twice held, for purposes of *Younger/Middlesex*, that states have an important interest in regulating their domestic insurers. *See Allegheny Corp. v. Pomeroy*, 898 F.2d 1314, 1318 (8th Cir. 1990); *McCartney*, 896 F.2d at 1144.

Finally, with regard to the third *Middlesex* factor, Warmus maintains that he had no opportunity to bring a civil rights action against appellees within the confines of AFSLIC's rehabilitation proceeding. *See Middlesex*, 457 U.S. at 432. We note, however, that AFSLIC, which is one and the same as Warmus for *Younger* purposes, *see Doran*, 422 U.S. at 928, attempted to bring a [sic] such an action in its rehabilitation. In May 1993, it filed a "Motion for Authority to File Suit on Behalf of Defendant" in the Circuit Court of Cole County, asking the court for permission to file a civil rights action against appellees and "possibly other present and former employees of [MDI]." Its attempt fell short when the court denied its motion. Rather than appealing this denial, AFSLIC deferred to Warmus's filing of the instant action in the district court. We agree with appellees that this amounted to an improper detour of the state's opportunity to address the constitutional claims against appellees. *See Huffman v. Pursue, Ltd.*, 420 U.S. 592, 609 (1975) ("a necessary concomitant of *Younger* is that a party . . . must exhaust his state appellate remedies before seeking relief in the district court); *McCartney*, 896 F.2d at 1144 ("a party cannot avoid *Younger* by choosing not to pursue available state appellate remedies").

We therefore hold that the third *Middlesex* factor, like the first two such factors, is satisfied, and conclude the district court did not abuse its discretion by choosing to abstain under *Younger*.

II.

Alternatively, appellees ask this court to affirm the judgment of the district court on grounds of qualified immunity, a defense which was raised but not addressed in the district court. Because we hold the district court properly abstained on the basis of *Younger*, we decline to reach the topic of qualified immunity.

III.

For the foregoing reasons, the judgment of the district court is affirmed.

A true copy.

Attest:

CLERK, U. S. COURT OF APPEALS, EIGHTH CIRCUIT.

IN THE UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF MISSOURI
CENTRAL DIVISION

THOMAS A. WARMUS, Plaintiff,	)	
vs.	)	No. 93-4306-CV-C-5
LEWIS MELAHN, et al., Defendants.	)	

ORDER

(Filed Nov. 29, 1993)

Before this Court are defendants' motion to dismiss, plaintiff's suggestions in opposition to the motion and defendants' reply to plaintiff's suggestions. For the reasons set out below, defendants' motion will be granted.

BACKGROUND

Plaintiff Warmus is the "beneficial owner, president and director of American Financial Security Life Insurance Company." Defendant Melahn is the former director of the Missouri Department of Insurance (MDI). Defendant Oetting is the former Chief Financial Examiner of the MDI. In early 1992, Melahn placed American Financial Security Life Insurance Company (AFSLIC) into Administrative Supervision, and eventually, in February, 1993, filed a petition in state court to have the company placed in rehabilitation status. Defendant Hobbs was appointed and acted as the Administrative Supervisor of AFSLIC. The state court appointed a special master to

hear the matter, and on March 18, 1993 issued an Order of Rehabilitation, finding that officials of MDI had "proved grounds sufficient to place . . . AFSLIC into rehabilitation pursuant to Section 375.1165 R.S.Mo. because AFSLIC is operating in hazardous condition." The Order further stated that ". . . AFSLIC and its officers, directors, managers, agents and employees are enjoined from disposition of its property and from the transaction of any of its business except as directed in writing by [the Director of the Missouri Division of Insurance]."

According to plaintiff, while his company was in Administrative Supervision status, before the petition for rehabilitation was filed, "virtually any actions taken in the continuing operations of AFSLIC . . . required the prior approval of the Director of Insurance or his appointed supervisor." This lawsuit challenges the activities of the defendants during that time, when AFSLIC was in Administrative Supervision. Plaintiff contends that the defendants conspired together in a direct attempt to "destroy the company and drive [plaintiff] out of the insurance industry." Specifically, plaintiff contends that the defendants misled him into believing that they approved of a certain reinsurance treaty he formed with another company and of the accounting methodology he was using. According to the Complaint, defendants knew that they would not ultimately approve the accounting methodology or the treaty, but kept silent about those facts in an attempt to "deceive and mislead [plaintiff] into a false sense of security, and . . . to deceive [plaintiff] into believing that [the treaty and the methodology] were acceptable so as to prevent [plaintiff] from taking other steps to secure a different type of reinsurance treaty or to

correct the concerns of MDI." Plaintiff's Complaint is in Four Counts. Count One states a claim for violation of his civil rights in that he alleges the defendants' actions violated his right to access to the courts and also that their actions deprived him of his property without due process of law. Counts Two, Three and Four claim, respectively, Abuse of Process, Breach of Fiduciary Duty and Prima Facie Tort.

ANALYSIS

Defendants, in their motion to dismiss, make the following arguments in favor of dismissal: 1) *Younger* abstention is appropriate; 2) plaintiff is estopped from bringing this suit by a ruling of the state court in which the court denied AFSLIC permission to sue the defendants; and 3) defendants are immune from liability. This Court finds that *Younger* abstention is appropriate and thus will not address defendants' other arguments.

Under the law as set out in the case of *Younger v. Harris*, 401 U.S. 37 (1941), and refined by the decision of *Middlesex County Ethics Committee v. Garden State Bar Association*, 457 U.S. 423 (1982), a federal court may decline to exercise its jurisdiction if: 1) there is an ongoing parallel proceeding in state court; 2) important State interests are implicated; and 3) there is an adequate opportunity to raise constitutional issues in the state court proceeding. *Alleghany Corp. v. McCartney*, 896 F.2d 1138, 1141, 1142 (8th Cir. 1990). In *Alleghany*, the Eighth Circuit noted that "federal courts have a 'virtually unflagging obligation' to exercise their jurisdiction." 896

F.2d at 1142 (citations omitted). The court went on to explain the concept of *Younger* abstention:

> This exercise of jurisdiction is constrained, however, by traditional principles of equity, comity, and federalism. . . . *Younger* abstention promotes the interests of both state and federal governments. As the Court announced in *Younger*, "[T]he National Government, anxious though it may be to vindicate and protect federal rights and federal interests, always endeavors to do so in ways that will not unduly interfere with the legitimate activities of the States."

896 F.2d at 1142 (citations omitted).

In determining whether abstention is appropriate, this Court first must determine whether there is an ongoing state proceeding. Clearly, there is such a proceeding. The plaintiff in this case has appealed the state court's decision that his company was operating in a hazardous condition and was properly placed into rehabilitation status. Although plaintiff attempts to make a distinction between this case and the one in state court, the distinction is not well taken. The issues he presents in this case are all directly related to the state proceedings, and if he were successful on appeal in the state proceedings then his claims in this Court would be moot. Furthermore, since plaintiff is the beneficial owner of AFSLIC, his interests and those of the corporation are identical.

The second inquiry under *Younger* is whether there is an important state interest implicated. Here, the validity and integrity of the state court's ruling is directly related to the issue of whether plaintiff's allegations about defendants are true. Furthermore, the State of Missouri has a

strong, recognized interest in the regulation of the insurance industry. *See*, 15 U.S.C. §§ 1011, 1012. Plaintiff contends that "[n]othing which is being requested of this Court would affect, in the slightest, the State Court's proceedings or any State interest." This Court disagrees and finds that important State interests are implicated.

The third factor to consider is whether there is an adequate opportunity to raise constitutional challenges in the state proceedings. Plaintiff argues that

> [t]he issues of the rehabilitation case are completely separate from the issues of the present case. Whether or not [plaintiff's] constitutional rights were violated were not material to whether AFSLIC violated any of the statutory grounds necessary to be placed into rehabilitation. [sic] The issues in this case were not raised in the rehabilitation case because the issues are not the same in both cases. Thus, there was no opportunity to raise such issues.

Plaintiff has failed to convince this Court that he could not raise the issue of defendants' alleged conduct on appeal. If, as he claims, defendants intentionally encouraged and lured him into operating his company in such a way that it was subject to being placed in rehabilitation status, and if such conduct amounted to a violation of plaintiff's constitutional rights, then it seems logical and appropriate to bring such facts to the attention of the appellate court reviewing the propriety of the state rehabilitation order.

Younger abstention is appropriate and plaintiff should raise his constitutional claims in the state court proceeding. Furthermore, this Court declines to exercise supplemental jurisdiction over plaintiff's state law claims, thus defendants' motion to dismiss will be granted.

Accordingly, it is hereby

ORDERED that defendants' motion to dismiss (doc. #14) is granted. The above-styled cause of action is dismissed, with prejudice.

/s/ Scott O. Wright
SCOTT O. WRIGHT
Senior United States
District Judge

November 29, 1993.

IN THE CIRCUIT COURT OF COLE COUNTY
STATE OF MISSOURI

JAY ANGOFF, Director, Department of Insurance State of Missouri, Plaintiff, v. AMERICAN FINANCIAL SECURITY LIFE INSURANCE COMPANY, Defendant.	)	Case No. CV193-10

SPECIAL MASTER'S REPORT TO THE COURT

Comes now James P. Dalton, appointed as Special Master by the Court on the 8th of February, 1993, pursuant to § 375.610, et seq. R.S.Mo. and makes the following report.

Pursuant to the Court's Order of Reference the Special Master commenced hearings on the matter referred on February 17, 1993 and concluded the hearings on March 1, 1993.

During the hearing, testimony of eleven witness [sic] was heard and 108 exhibits introduced. The transcript of the hearing covered in excess of 1,500 pages.

Per the Order of Reference the Transcript and Exhibits have been filed with the Court.

General Background Information

The Defendant, American Financial Security Life Insurance Company is a Missouri domiciled life insurance company.

On March 6, 1992 the Director of the Missouri Department of Insurance Issued an Order of Administrative Supervision pursuant to § 375.1160 R.S.Mo. citing that various conditions existed that made the company's continued business hazardous to the public and the company insureds.

The Order of Administrative Supervision set forth eleven (11) activities American Financial Security Life Insurance Company could not do without the prior approval of the Director of Insurance or his appointed supervisor and further appointed such supervisor.

Attached to the Order was a List of Requirements to Rescind Determination of Administrative Supervision. There were six (6) such requirements.

The Order of Administrative Supervision was extended periodically through December 30, 1992.

On February 1, 1993 the present case was commenced by the Director of Insurance filing a Verified Petition For Rehabilitation of American Financial Security Life Insurance Company.

The Verified Petition For Rehabilitation set forth in eight (8) separate counts the Director's alleged grounds for placing American Financial Security Life Insurance Company in rehabilitation.

Among other requests the prayer of such count prayed for an order of rehabilitation under § 375.1165 through 375.1166 R.S.Mo. and such other orders and relief under § 375.1150 to 375.1246 R.S.Mo. as shall be found advisable or necessary.

As specific evidence adduced at the hearings related in many instances to more than one count in the petition to set forth findings of fact separately relating to each such count would be repetitious and unwarranted. Each count in Plaintiff's petition is addressed individually in the Conclusions of Law.

Findings of Fact

1. These proceedings are instituted by verified petition of the Director of the Department of Insurance of the State of Missouri (Plaintiff) who requests that American Financial Security Life Insurance Company (AFSLIC) be placed in rehabilitation.

2. Plaintiff, JAY ANGOFF, (ANGOFF) is the Director of the Department of Insurance for the State of Missouri.

3. This action was commenced by LEWIS MELAHN, (MELAHN) (ANGOFF's predecessor), as Director of the Department of Insurance for the State of Missouri.

4. Plaintiff, in February 1992, filed with the Court a stipulation that he would introduce an examination report regarding the condition and affairs of Defendant as Plaintiff's case in chief. Plaintiff introduced the Report of Examination of AFSLIC as of September 30, 1992 as Plaintiff's Exhibit 1.

5. Defendant, AFSLIC, is an insurance company organized under the laws of the State of Missouri.

6. AFSLIC was incorporated as Survivors Benefit Life Insurance Company in 1957, as a stipulated premium company under the Insurance Laws of the State of Missouri. (Plaintiff's Exhibit 1, Page 5)

7. In 1980 the Company was acquired by PENN MUTUAL LIFE INSURANCE COMPANY, who in 1981 adopted the name, PENN DIVERSIFIED INSURANCE AND ANNUITY COMPANY. (Plaintiff's Exhibit 1, Page 5)

8. On May 2, 1989, AMERICAN WAY HOLDINGS INC. (HOLDING) purchased the Company and on May 17, 1989 changed its name to AFSLIC (Plaintiff's Exhibit 1, Page 5)

9. AFSLIC is currently operating as a stock, life company under Chapter 376 RSMo, and is authorized to write life, annuities and endowments, accident and health and variable contracts. (Plaintiff's Exhibit 1, Page 5)

10. AFSLIC is a member of a holding company system controlled by Thomas Warmus (WARMUS), which is made up of seven insurance companies and three non-insurance companies. (Plaintiff's Exhibit 1, Page 8, Tr 87-92)

11. When HOLDING acquired AFSLIC, some of its policyholders were residents of Missouri. Some of these same Missouri residents are policyholders today. (Tr 693, 694)

12. All Missouri policyholders pay their premiums directly to AFSLIC (Tr 694, 502, 503), and have done so since the Company was acquired.

13. From the time the Company was acquired AFSLIC has not sold any insurance contracts covering credit life, disability, whole life or any other policy to residents of the State of Missouri. (Tr 694)

14. In 1989, WARMUS discussed with the MDI its plans to streamline the holding company system, move the credit insurance business of his Michigan company to AFSLIC and make AFSLIC the "flagship" of the holding company system. (Tr 691, Plaintiff's Exhibit 29)

15. Before AFSLIC could commence issuing credit insurance policies in Michigan, it was required to have its policies, premiums and agency contracts approved by the appropriate regulatory authorities. This process was not completed until 1991. (Tr 692)

16. AFSLIC began receiving premiums from Michigan residents in January 1992. (Tr 1439)

17. The premiums which AFSLIC began receiving in January 1992 was from a book of business covering credit life, accident and health policies being written by agents affiliated with automobile dealers, who sold this coverage to motor vehicle customers when an automobile sold was financed. These agents had previously placed their credit life and disability insurance in AMERICAN WAY LIFE INSURANCE COMPANY (LIFE), a Michigan affiliate. (Tr 112-114)

18. The transfer of business from LIFE to AFSLIC was part of a long range plan which was previously

discussed with MDI in 1989; however, the actual transfer date was accelerated by regulatory actions taken by the Michigan Insurance Bureau. (Tr 692, 664)

19. Currently 99% of AFSLIC's insurance is being written as credit life and credit disability insurance in the State of Michigan. (Plaintiff's Exhibit 1, Page 12)

20. On March 6, 1992, Plaintiff issued an Order For Administrative Supervision against AFSLIC pursuant to §376.1160 RSMO. That Order recited that the Defendant's condition rendered the continuation of its business hazardous to the public or its insureds because:

a. AFSLIC was associated with American Way Life Insurance Company (LIFE) and AMERICAN WAY CASUALTY COMPANY (CASUALTY); both of Michigan; which the Order of Administrative Supervision claimed were "insolvent and in a hazardous condition", and

b. AFSLIC was transacting business to a much greater extent than it did prior to November 1991, without a corresponding increase in its policyholder's surplus. (Plaintiff's Exhibit 3)

21. The Order also provided that AFSLIC not do any of the following things during the period of supervision, without the prior approval of his appointed supervisor to-wit:

a. Dispose of, convey or encumber any of your assets or your business in force;

b. Withdraw any of your bank accounts;

c. Lend any of your funds;

d. Invest any of your funds;

e. Transfer any of your property;

f. Incur any debt, obligation or liability;

g. Merge or consolidate with another company;

h. Approve new premiums or renew any policies;

i. Enter into any new reinsurance contract or treaty;

j. Make any material change in management; or

k. Increase salaries and benefits of officers or directors or the preferential payment of bonuses, dividends or other payments deemed preferential.

22. Attached to the order of Administrative Supervision was a "List of Requirements To Rescind Determination Of Administrative Supervision" which contained the following six requirements:

a. Arrange for any necessary reinsurance with unaffiliated licensed insurers licensed in the State of Missouri;

b. Collect all inter-company receivables within 10 days;

c. Submit monthly Balance Sheets, Income Statements and cash Flow Statements to Plaintiff on the 21st day of each month;

d. Document all other invested assets;

e. Obtain a certification from the Michigan Insurance Bureau that American Way Insurance Company and American Way Casualty

of Michigan are solvent and not in a hazardous condition;

f. Reduce premiums so that AFSLIC maintains a ratio of premium to surplus of no more than 3 to 1, or such other ratio as Plaintiff or his Supervisor may permit. (Plaintiff's Exhibit 3)

23. Originally, MELAHN appointed Joseph Fink as Administrative Supervisor. (Plaintiff's Exhibit 3)

24. On May 4, 1992, Plaintiff extended the order of Supervision and Plaintiff appointed WILLIAM R. HOBBS (HOBBS) to replace Joseph Fink as Administrative Supervisor. (Tr 1347, Plaintiff's Exhibit 3)

25. HOBBS remained in his capacity as Administrative Supervisor throughout the supervision. (Tr 1152)

26. Plaintiff originally sent financial examiners to AFSLIC in February 1992 to examine AFSLIC's financial condition as of December 31, 1991. Examiners remained on the premises of AFSLIC through the end of July 1992. The examination as of December 31, 1991, was never completed; instead, plaintiff sent the examiners back in December 1992 to update the examination to September 30, 1992. (Tr 1286-1288)

27. The examiners completed their examination on December 30, 1992, and left the premises of AFSLIC without communicating their results to AFSLIC and without holding a customary Exit Conference. This was done because the examiners knew prior to December 25, 1992, that MDI would be taking regulatory action against AFSLIC. (Tr 1357-1359)

28. On January 7, 1993, AFSLIC was served with an Ex Parte Seizure Order obtained by plaintiff, pursuant to §375.1164 RSMO seizing AFSLIC's assets and enjoining it from further conducting its business except with Plaintiff's written consent. (Tr 1360)

29. One day later on January 8, 1993, Defendant received a copy of the Examination Report for the period ending September 30, 1992, with a cover page giving Defendant thirty days to file exceptions or objections to the report. (Defendant's Exhibit 1)

30. Within thirty days, Defendants filed their response to the Examination Report and requested that it be made a part of the public record. (Defendant's Exhibit 30)

31. On February 1, 1993, prior to the time that a response to the Examination Report was due, Plaintiff filed the instant Verified Petition For Rehabilitation pursuant to §375.1165 RSMo and obtained an Ex Parte Preliminary Order authorizing him to take charge of AFSLIC's assets and property.

32. The Verified Petition For Rehabilitation filed by Plaintiff against AFSLIC contained eight counts:

a. Count I is based upon the allegations that the premium to surplus ratio is excessive;

b. Count II is based on the allegation that AFSLIC failed to provide loss reserve credits for reinsurance ceded and thereby overstated its surplus;

c. Count III is based on the allegation that the Company's assets do not exceed its liabilities plus the capital and surplus required by Missouri Statutes;

d. Count IV is based on the allegation that AFSLIC violated a valid order of the Administrative Supervision to write no more than 1.4 million dollars of premium, per month, or exceed a ratio of premium to surplus of 3 to 1.

e. Count V is based on the allegation that AFSLIC failed to file an audited Financial Report on or before May 1, 1992;

f. Count VI is based on the allegation that AFSLIC's condition and affairs continued to deteriorate since the entry of a Seizure Order;

g. Count VII is based upon the allegation that AFSLIC violated Missouri laws §375.925.2 RSMo by failing to have a written agreement which specifies the fiduciary duties of its alleged administrator, American Way Service Corporation;

h. Count VIII is based upon the allegation that AFSLIC refused to release 1991 financial information on any of the non-insurance affiliates, in violation of §374.190 RSMo.

33. AFSLIC filed their Answer and Affirmative Defenses to the Verified Petition For Rehabilitation denying any and all wrongdoing and violations of Missouri Statutes or Order of the Plaintiff.

34. Upon the return date of the Summons, this matter was set for hearing before the Honorable James P. Dalton, Special Master.

35. Pursuant to §375.610 RSMO, Plaintiff stipulated that its case in chief would consist solely of the Examination Report as of September 30, 1992. AFSLIC was permitted no discovery.

36. The hearing commenced on February 18, 1993 and concluded on March 1, 1993.

37. Plaintiff introduced a certified copy of its examination of AFSLIC as of September 30, 1992. (Plaintiff's Exhibit 1)

38. According to the Missouri Department of Insurance ("MDI") Report of Examination AFSLIC had capital and surplus of negative $5,423,852 on September 30, 1992. (Plaintiff's Exhibit 1, p. 21.)

39. In calculating these figures, the MDI disallowed a receivable from an AFSLIC affiliate shown as an asset on the AFSLIC September 30, 1992 quarterly financial statement, in the sum of $939,286. (Plaintiff's Exhibit 1, p. 24.)

40. The inclusion or exclusion of the $939,286 asset would have no material effect on the ultimate findings as to AFSLIC being placed into rehabilitation. (Plaintiff's Exhibit 1, p. 21.)

41. Under the statutory accounting rules that are utilized by MDI for the reporting of financial conditions for insurance companies, credit insurance possesses unique characteristics. A company like AFSLIC which sells single premium credit insurance is initially required

to maintain reserves on its balance sheet equal to one hundred percent of its premiums for accident and health insurance, and eighty-five percent for credit life insurance. (Tr 144)

42. These reserves decrease as the policy matures. (Tr 161-163)

43. These reserving procedures must be followed even though AFSLIC's book of business has a well established historical loss ratio of only thirty-five percent. (Tr 144)

44. Additionally, the Company pays commission at the time the certificate of insurance is issued in the amount of fifty percent. This commission rate is standard in the industry. AFSLIC is required to recognize its commissions as an expense on the year they are paid and is not allowed to amortize them across the life of the policy. (Tr 792)

45. The commission payments create an immediate surplus strain for AFSLIC which reduces the reported capital and surplus in the initial years, even though the business will most likely be profitable in the long run. (Plaintiff's Exhibit 1, Page 13, Tr 1313)

46. The issue concerning the amounts of reinsurance which AFSLIC is entitled to take as a reserve credit on its Balance Sheet is by far the single most important issue in this case and is critical to a determination of Counts I, II, III, and IV of Plaintiff's Petition.

47. Absent an approximate 8 million dollar reserve credit as might be allowed under a reinsurance treaty with Lloyds of London, AFSLIC would have negative

capital and surplus of approximately 5 million dollars as of September 30, 1992. (Plaintiff's Exhibit 1, p. 22, 23.)

48. AFSLIC commenced its search for reinsurance in 1991 when it began contemplating the transfer of the Michigan credit life and credit disability insurance business from LIFE to AFSLIC. (Tr 900)

49. MELAHN, HOBBS, and AFSLIC all believed that proper reinsurance could resolve the initial surplus strain on the Company as well as the Plaintiff's concern regarding the ratio of premiums to surplus. (Tr 346, 546,572,667,890,1172)

50. AFSLIC could not enter into Reinsurance Contracts after the date of the Order of Supervision dated March 6, 1992 without the approval of the Director or his "appointed supervisor." (Plaintiff's Exhibit 3)

51. JAY JAFFE (JAFFE), the actuary whom AFSLIC chose to use in its search for reinsurance had been in the credit life disability insurance for over twenty years, was familiar with the business that the company was writing because he had worked as an actuary on American Way's business from the mid 70's through 1986. (Tr 192,194)

52. From the inception, JAFFE believed that the approval of Plaintiff was mandatory in the search for acceptable reinsurance and that the MDI had to be kept involved and aware. (Tr 201)

53. JAFFEE submitted a proposal from Lloyd's of London (Lloyds). (Tr 196)

54. Lloyds as well as its underwriters who eventually decided to participate in reinsuring AFSLIC were proper and acceptable in Missouri. (Tr 1090)

55. Pursuant to the Order of Administrative Supervision and its extensions, HOBBS was the only person besides MELAHN, who had the authority to approve entering into a reinsurance contract with AFSLIC. Therefore, HOBBS was the only representative of MDI with whom AFSLIC communicated regarding the approval of the Lloyd's Reinsurance Treaty. (Plaintiff's Exhibit 3, Tr 955)

56. A central, but not the sole issue, in determining whether to approve the Lloyd's Treaty was the accounting methodology which determined what would be the appropriate amount of reserve credits, if any, that the ceding insurer would be permitted to take on its Balance Sheet. (Tr 256, 348, 811, 1206)

57. Every two weeks throughout the time which HOBBS served as an Administrative Supervisor of AFSLIC, HOBBS sent written reports to JAMES OETTING (OETTING), the Chief Financial Examiner of MDI throughout the supervision, with a copy to MELAHN in order to keep them advised of all significant developments with AFSLIC (Tr 1166)

58. In addition to the bi-monthly written reports, HOBBS communicated orally with MELAHN and OETTING an average of four or five times per month. (Tr 1220)

59. Throughout the Administrative Supervision, HOBBS and personnel at AFSLIC maintained a friendly relationship that was not adversarial. (Tr 1204, line 8)

60. The first reinsurance treaty which was presented to HOBBS from Lloyds was rejected because HOBBS felt there was no transfer of risk. (Tr 1034)

61. In June, 1992 a subsequent cover note for a Lloyds Treaty was obtained from Lloyds. (Tr 1034, 1035)

62. On June 24, 1992, AFSLIC sent HOBBS and ROBIN MARCOTTE, (MARCOTTE) the Missouri examiner in charge of the examination of the company, two different projections concerning the subsequent Lloyds Treaty which included the amount of premiums expected to be written and the amount of reserve credits which the company would expect to recover. Attached to the projections prepared by AFSLIC, was a copy of a letter from JAFFE describing the Lloyd's coverage, the premium calculation and the calculation of reserve credits. The projections were based upon the assumption that AFSLIC would be writing $2,500,000 per month, and that the credits which the company would receive for the nine months of coverage of April 1, 1992 through December, 1992 would be in excess of $9 million. (Defendant's Exhibit 34 and Defendant's Exhibit 35)

63. HOBBS did not object to either the amount of premium which was proposed to be written, or to the credits proposed to be taken by the Company.

64. Two days later, on June 26, 1992, HOBBS wrote to DAVID HOWARD (HOWARD), the Controller of AFSLIC, stating that after discussions with OETTING, MDI would give serious consideration to approving a reinsurance treaty between AFSLIC and Lloyd's along the terms which they have been discussing. HOBBS expressed a desire to review, "the proposed treaty and

the projections of income and reserve credits under the treaty." HOBBS requested that HOWARD send him a copy of the proposed treaty, a description of the method for calculating reserve credits, and projected financial impact for 1992 and 1993. Finally in the June 26, 1992 letter, HOBBS advised that it would be necessary to obtain an independent actuarial opinion with regard to "reserve calculation and proposed statutory reinsurance credit." (Defendant's exhibit 18)

65. On July 8, 1992, JAFFE sent a letter to HOBBS enclosing a specimen copy of the cover note showing that the maximum sum insured would be up to $25 million for a period of nine months (April, 1992 through December, 1992) together with a sample reinsurance contract and an explanation of the reserving methodology. (Defendant's Exhibit 9)

66. HOBBS choose [sic] the actuary, SAM GUTTERMAN (GUTTERMAN) from the firm of Price Waterhouse to review the accounting methodology of the proposed treaty with Lloyds and to ascertain if there was a transfer of risk. (Tr 349)

67. GUTTERMAN in his evaluation of the proposed Lloyd's Reinsurance Treaty found that there was a transfer of risk and that the reserve methodology was correct, wit some adjustments. (Defendant's Exhibit 10)

68. AFSLIC made the adjustments suggested in GUTTERMAN's report and reflected those adjustments in both the June and September Quarterly Reports. (Tr 351)

69. On July 20, 1992, HOBBS wrote to OETTING with a copy to MELAHN in which HOBBS attached a

copy of the specimen Reinsurance Treaty, stating that "there does not seem to be any reason to deny the company's request", HOBBS concluded that the agreement will provide "true risk transfer for reasonable cost", and described the coverage as "the reinsurer assumes the responsibility for all premium refunds and claims paid during the three year period in excess of 45% of earned premium up to a maximum of 100%". (Defendant's Exhibit 19)

70. On August 3, 1992, HOBBS approved the Reinsurance Contract with Lloyds. (Defendant's Exhibit 20)

71. Two days later on August 5, 1992, HOBBS wrote another report to OETTING, with a copy of MELAHN which stated, "per my discussion with Lew on Monday, I have provided the company with approval (copy attached) to complete a reinsurance treaty with Lloyds". (Defendant's Exhibit 44)

72. In his August 5, 1992 Report to OETTING and MELAHN, HOBBS estimated that with the Lloyds Treaty in effect and assuming $26 million in written premium, that year end capital and surplus would be about 3.3 million dollars. (Defendant's Exhibit 44) In estimating the year end premium and surplus, HOBBS used reserve credits from both Lloyd's Reinsurance Treaty as well as a Reinsurance Treaty with American Trend Life Insurance Company (AMERICAN TREND). (Tr 1186)

73. AMERICAN TREND was an insurer domiciled in the State of Arizona and an affiliated company of AFSLIC; however, was not authorized as a reinsurer in the State of Missouri. (Tr 91,1184,1185)

74. AFSLIC relying upon correspondence it received from MELAHN reasonably believed that it could take credits for reinsurance ceded to AMERICAN TREND for all statements filed in 1992, except the statement filed for December 31, 1992. (Defendant's Exhibit 61, Tr 1183)

HOBBS knew about the existence of AMERICAN TREND, since the date he commenced his duties as Administrative Supervisor in May 1992. By the end of August 1992, at the very latest, HOBBS knew that AMERICAN TREND was not authorized as a reinsurer in the State of Missouri. (Tr 1180,1181)

76. Until October 21, 1992, HOBBS did not object to AFSLIC receiving credit for reinsurance ceded to AMERICAN TREND. (Tr 1183, Defendant's Exhibit 63)

77. The Lloyds Treaty covered policies written by AFSLIC from April 1, 1992 until December 31, 1992 for a period of three years after December 31, 1992. It paid claims and gross refunds of premiums up to a maximum of fifty five percent of unearned premium reserves as of December 31, 1992, or the treaty limit, whichever was smaller. Lloyds would be obligated to pay after its attachment point is reached, which is subsequent to the exhaustion of the company's retention of forty five percent of the unearned premium reserves. The liability of Lloyds decreased parallel to the decrease in the company liability, pursuant to Statutory Accounting Rules. (Defendant's Exhibit 31, Defendant's Exhibit 10, Defendant's Exhibit 49, T 226)

78. On August 11, 1992, HOBBS authorized payment of the initial premium of $250,000 to the Lloyds broker, INBRO CITYGATE LIMITED. The limit on the

Treaty was 25 million for 9 months. (Defendant's Exhibit 22)

79. Late in August the limit on the treaty was reduced to $18,750,000, which resulted in the initial premium payment being reduced to $200,000. (Tr 378)

80. On August 20, 1992, HOBBS advised AFSLIC's actuary, DAVID KUNESH in writing, that the Reinsurance Treaty had been approved by him as "Administrator Supervisor" of AFSLIC. In that letter HOBBS also specifically approved the company's inclusion of the reserve credits for the Lloyds Treaty on its June 30th Statement. (Defendant's Exhibit 21)

81. On August 25, 1992, HOBBS in his progress report to OETTING, with a copy to MELAHN, advised them that the maximum coverage on the Lloyds Treaty would only be $18,750,000 instead of the $25 million because HOBBS was advised that one of the other underwriters was "scared off by the Missouri Order of Supervision". (Defendant's Exhibit 26)

82. On September 16, 1992, HOBBS sent his progress report on AFSLIC to OETTING with a copy to MELAHN. In that letter he revealed that he discussed the reinsurance treaty with ROBERT BAILEY (BAILEY), the Deputy Commissioner of Michigan, and that BAILEY did not agree with the accounting methodology. HOBBS stated "I am uncertain of the correct conclusion and plan to discuss it further with you". (Defendant's Exhibit 46, T-704)

83. HOBBS did not discuss his uncertainty with the accounting methodology with AFSLIC and did not advise

the company of BAILEY's opinion of the accounting methodology. (TR 1089 and Defendant's Exhibit 46)

84. On September 21, 1992, HOBBS in his report to OETTING together with a copy to MELAHN, stated that he needed to discuss the method of calculating reserve credits on the Lloyds Treaty with the company; however, he still had not advised AFSLIC either in writing or orally of MDI's questioning the accounting treatment on the Lloyds Treaty. (Plaintiff's Exhibit 18)

85. By September or October 1992, OETTING discussed the Lloyds Treaty with BAILEY, and OETTING concluded that the company should receive no credits for the Lloyds Treaty. OETTING did not communicate his opinion to AFSLIC either in writing or orally at any time during 1992. (Tr 1515)

86. On October 20, 1992, HOWARD sent HOBBS a draft of the proposed Quarterly Statement for the period ending September 30, 1992, which was required to be filed approximately one month later. (Defendant's Exhibit 38)

87. On the Preliminary Quarterly Statement for September 1992, the company took full credit for the Lloyds Treaty.

88. The next day, October 21, 1992, HOBBS advised HOWARD that HOBBS disapproved of the taking of the reinsurance credits for the treaty between AFSLIC and AMERICAN TREND on the June Quarterly Statement. At no time did HOBBS question the credits taken for the Lloyd's Treaty. (Tr 1200)

89. Even though AFSLIC had the right to use the AMERICAN TREND treaty and receive credits on the statements until December 1992, it complied with the wishes of HOBBS and did not use the credits from AMERICAN TREND in its September Quarterly Statement instead, AFSLIC obtained the consent of Lloyds to change their coverage from the last nine months of 1992 to the first nine months of 1992, and started to look for additional reinsurance from an authorized reinsurer for the last Quarter of 1992. (Defendant's Exhibit 61,23,32,33)

90. Lloyds did not care which nine month period in 1992 they insured so long as the maximum amount of coverage did not change. (Defendant's Exhibit 75, 76)

91. The change of coverage from the last nine months of 1992 to the first nine months of 1992 on the proposed Lloyds Treaty was not approved by Hobbs until December 8, 1992. (Defendant's Exhibit 33)

92. No evidence was presented that would indicate that the decision to change the Lloyds Treaty date covering the last nine months of 1992 to the first nine months of 1992 was anything other than a voluntary and conscious act of AFSLIC.

93. On November 16, 1992, HOWARD wrote HOBBS confirming a recent conversation with him in which HOBBS was advised that the company planned to file its September 30 Financial by amending the Lloyd's insurance to cover the period from January 1st through September 30, 1992, cancelling the life treaty with AMERICAN TREND and taking no credit on the disability aspect of the treaty with AMERICAN TREND. The Company proposed to obtain disability reinsurance with an

unaffiliated company for the last quarter of the year subject to division approval. Lloyds had previously confirmed that they would move the coverage period to cover the first nine months of the year instead of the last nine months of the year. In the November 16th letter, HOWARD explained how the credits for the Lloyds Treaty as revised would be reflected on AFSLIC September 30th Quarterly and asked for approval for this methodology. (Defendant's Exhibit 23)

94. There was never a written response from HOBBS to this request or correspondence from HOBBS to either AFSLIC, MELAHN or OETTING stating the HOBBS disapproved the inclusions of the revision to the Lloyds Treaty on AFSLIC's September 30, 1992, Financial. (Tr 1200)

95. No one from MDI indicated any disapproval of the September 30, 1992 Financial Statement through the end of 1992.

96. On December 1, 1992, HOWARD again wrote HOBBS regarding the change in Lloyds, requested formal approval and advised him once again, that the changes were reflected in the Company's Third Quarter Financial Statement. HOBBS sent a copy of the December 1, 1992 to MDI with his hand-written notations "both seem okay in principal". [sic] (Defendant's Exhibit 32)

97. On December 8, 1992, HOBBS wrote HOWARD stating he had no objection to the amendment of the dates on the Lloyds Treaty, HOBBS makes no objections to its inclusion on the Financial Statement dated September 30, 1992. (Defendant's Exhibit 33)

98. AFSLIC, on its September 30, 1992 Quarterly Statement, using its own methodology and the coverage dates of January 1992 through September 1992 under the Lloyds Treaty took a reserve credit of approximately $8,274,000 which resulted in a capital and surplus of slightly less than $3,000,000. (Defendant's Exhibit 37, Tr 1066-1069)

99. The inclusion of Lloyds Treaty reserve credit of approximately 8 million dollars on its September 30th Quarterly Statement was not authorized under the Lloyds Treaty as its terms that existed on September 30th covered April through December 1992. Using the coverage dates of April through December would permit only a 5 million dollar reserve credit using AFSLIC's methodology and a resulting capital and surplus of zero or below and below the minimums permitted by statute. (Tr 1055-1071)

100. The Lloyds Treaty cover note received shortly after October 15, 1992 showed a coverage date of April through December 1992. (Defendant's Exhibit 31)

101. Even though Lloyds did not object to a change in coverage dates and HOBBS did not object to the same no cover note or no final reinsurance treaty was issued covering the period of January 1992 through September 1992 as used for AFSLIC's September 30th Quarterly Statement.

102. The Reinsurance Policy finally issued by Lloyds shows coverage for the last 9 months of 1992 (April through December) and is the best evidence as to the terms of Lloyds' obligations. (Defendant's Exhibit 79)

103. By using the coverage dates of January, 1992 through September, 1992 and its September 30, 1992 Quarterly Statement, AFSLIC overstated any surplus as regards policyholders.

104. The accounting methodology to calculate reserve credits under the Lloyds Treaty as used by AFSLIC is not acceptable to Plaintiff. (Plaintiff Exhibit 1)

105. Defendant's witness, JAFFE, a reinsurance intermediary and actuary approved the methodology. (Tr 213)

106. GUTTERMAN an independent actuary employed by the MDI approved the methodology with minor revision. (Defendant's Exhibit 10)

107. Dan Kunech, an actuary with AFSLIC's accounting firm approved the accounting methodology but did so conditionally. (Defendant's Exhibit 12)

108. The Department's actuary, GEORGE DAVIDSON, (DAVIDSON) issue a report on December 17, 1992 concluding that the accounting methodology required "further attention," and stating that "these questions should be directed to the actuaries involved in the design of the reinsurance treaty and the establishment of reserve credits under the treaty." (Defendant's Exhibit 51) Despite these preliminary findings there is no evidence that DAVIDSON ever spoke to GUTTERMAN or JAFFEE; however, FREDERICK HESSE (HESSE), an MDI employee who was the audit manager of the examination of AFSLIC, and HOBBS, spoke to GUTTERMAN in December, 1992. Even after this conversation with their own

chosen actuary, GUTTERMAN refused to change his opinion on the accounting method. (Tr 1221)

109. OETTING, former Chief Examiner of the MDI, had serious doubts about the accounting but appeared to partially base his belief on the opinion of BAILEY who's [sic] testimony is disregarded and at request of Plaintiff's counsel is given no consideration by this Special Master. (Tr 1463, 1467)

110. The Lloyds Treaty is unusual and not drafted along the lines more common treaties used in the industry. (Tr 249, 260, 803, 804)

111. The fact that the Lloyds Treaty is unusual is not in itself fatal to its use in calculating reserve credits.

112. The Lloyds Treaty provides protection for both AFSLIC and its insured. (Tr 247-249, 287, 294)

113. The Lloyds Treaty was more appropriate than conventional treaties for the type of business reinsured. (Tr 250)

114. The reinsurance treaty with Lloyds conferred a real benefit upon the company, seemed particularly applicable to the type of insurance that the Company wrote and adequately protected the policyholders. (Tr 224, 247, 294, 453, 908, 913, 916)

115. The greater weight of the evidence persuades this Special Master that the general accounting methodology used by AFSLIC was appropriate.

116. Historically reserve credit for nonproportional coverages of the nature of the Lloyds Treaty are generally not acceptable to State Regulators. (224)

117. AFSLIC is licensed in 44 states and the vast majority of its insurance is written in states other than Missouri. (Plaintiff's Exhibit 1.)

118. It was detrimental to AFSLIC for Plaintiff or Hobbs not to advise AFSLIC at the earliest time it became apparent that Plaintiff would not in the final analysis approve AFSLIC accounting methodology under the Lloyd's Treaty in taking reserve credits regardless of what period of 1992 was to be covered by the Treaty.

119. The failure of Plaintiff and/or Hobbs to advise AFSLIC of the pending methodology treatment was and is of such a serious nature that Plaintiff should not in good conscious [sic] exercise his discretion under the statutes and regulations and disapprove the methodology used by AFSLIC.

120. Regardless of this Special Master's findings, for AFSLIC to rely on the Lloyds Treaty and the accounting methodology, considering the diverse views of actuarial experts and state regulators, it would and does make business hazardous as the company's solvency is directly related to the accounting methodology and reserve credits permitted not only by Plaintiff but by insurance regulators of states in which Defendant is licensed.

121. The issue of whether Defendant's premium to surplus ratio was excessive is crucial to both Count I and Count IV of Plaintiff's Complaint.

122. One of the six requirements to rescind the rehabilitation order was to reduce premium writing in order

that AFSLIC "Maintains a ratio of annualized gross premiums written to policyholder surplus of no more than three to one, or such other ratio as Director or Supervisor may permit." (Plaintiff's Exhibit 3)

123. The 3 to 1 ratio is a standard applicable to casualty companies, and is not necessarily applicable to a life company which writes single premium credit, life and disability policies. (Tr 893, 894, 1452)

124. The level of premium writings can be reduced by either reducing premium volume, an infusion of capital, or through reinsurance. (Tr 1164)

125. A question arose whether in the ratio suggested in the requirements to rescind the order of rehabilitation, "annualized gross premiums" meant "adjusted gross", or whether it meant "net of reinsurance". On April 15, 1992, Plaintiff's counsel, NICHOLAS M. MONACO (MONACO), wrote MARK STAHLHUTH, General Counsel for Plaintiff, asking that very question. (Defendant's Exhibit 47) On April 17, 1992, the Chief Financial Examiner responded to that letter stating that irrespective of the definition, the company had exceeded the ratio and "no further business may be produced during the month of April." (Plaintiff's Exhibit 4)

126. On April 20, 1992, OETTING followed up his letter of three days earlier and again requested that business for the month of April cease. (Plaintiff's Exhibit 5)

127. Three days later on April 23, 1992, MONACO wrote OETTING asking him to reconsider his decision of April 17, and April 20, 1992, to allow the Company to

continue writing since cessation of writing would destroy the business. (Defendant's Exhibit 48)

128. On May 1, 1992, MELAHN responded to MONACO's April 23 letter in which the Director extensively discussed reinsurance and stated, "You are correct that AFSLIC is in an untenable situation. It is in this situation because the company has apparently chosen not to exercise any responsibilities toward the control and growth of this company, or in arranging for a proper reinsurance program". (Plaintiff's Exhibit 6)

129. Defendant reasonably interpreted MELAHN's May 1, 1992, letter to mean that MDI's concern with premium writings could be eliminated through reinsurance.

130. There was no further communication to the company by MDI subsequent to the May 1st, 1992 letter from MELAHN to MONACO regarding the level of premium writings until October 22, 1992 when STAHLHUTH wrote MONACO another letter claiming that AFSLIC wrote premiums in excess of MDI's requirement and stated, "Should Director issue an order requiring AFSLIC to write no more insurance business in order to obtain compliance with the administrative supervision order and prevent a delinquency proceeding?" (Plaintiff's Exhibit 15)

131. MONACO replied on October 26, 1992 and stated that due to reinsurance which the Company had acquired, it had not violated any requirements of suggested premium writing. (Defendant's Exhibit 58)

132. There were no follow ups to that letter.

133. During the entire administrative supervision, MDI was aware that the amount of business the company was writing was in excess of $1.4 million per month and had voiced no objection. In the discussions for approval of the reinsurance treaty, which was brought to the attention of HOBBS, OETTING and MELAHN, the amount of premiums which were sought to be covered was originally $25 million for nine months, which is well in excess of $1.4 million per month. There were no objections to the amount of the treaty and the company reasonably believed that writings in that monthly amount were acceptable.

134. In a letter from HOBBS to WARMUS dated August 3rd, 1992, when the amount of the treaty with Lloyds was still $25 million for 9 months, HOBBS instructed WARMUS, "Since the treaty has a maximum amount of coverage, the company must take steps to insure that business written during this period does not exceed the maximum." (Defendant's Exhibit 20)

135. Plaintiff clearly allowed AFSLIC to write at the level that it was writing of approximately 2.5 million per month and AFSLIC reasonably believed that it was fully complying with the desires of Plaintiff regarding the level of premium writings.

136. This Special Master is not convinced that the use of a 3 to 1 ratio is appropriate. The 3 to 1 ratio may be an industry standard for casualty insurance but is not statutorily required or necessarily applicable to credit life insurance. (Tr 1452, 1392)

137. AFSLIC presented convincing evidence from WARMUS, who has been in the industry for over thirty

years, that the 3 to 1 ratio is not appropriate for credit life insurance. (Tr 893, 894)

138. Documents obtained from MDI, indicated that for MDI's own internal purposes in conducting a financial analysis, MDI used ratios of 7 to 1 as a measuring standard. (Defendant's Exhibit 78)

139. AFSLIC did not violate any ORDER of the Plaintiff by exceeding a ratio of 3 to 1 as such was a condition for termination of the Order of Supervision.

140. The premium writings by AFSLIC were however excessive in relation to its premium and surplus level, as AFSLIC did not have at all times adequate reinsurance in place.

141. MDI complained that AFSLIC did not have a written agreement with AMERICAN WAY SERVICE (SERVICE).

142. AFSLIC asserted that SERVICE does not work for AFSLIC and a [sic] agreement is not required. Moreover, AFSLIC alleged that such an agreement would not make any sense.

143. The same persons service all companies in the group of companies comprising the AMERICAN WAY group which includes AFSLIC. These people are paid by each company allocating in advance an appropriate portion of the time that the employee works for the company. Each company pays its allocated share of salary, social security and other items. (Tr 93-107)

144. All salaries are paid by AMERICAN WAY LIFE INSURANCE COMPANY (LIFE) which is reimbursed its

appropriate share from other members of the group. (Tr 93)

145. When a person performs work for AFSLIC, he considers himself an employee of AFSLIC, and when someone performs work for another company, he considers himself an employee of that particular company. (Tr 93, 94)

146. Prior to the administrative supervision, premium checks on AFSLIC's Michigan business were deposited into a specimen account in the name of SERVICE. After the Supervision, they were deposited into a special joint account in the names of SERVICE and AFSLIC. (Tr 1298)

147. During the beginning months of 1992 there was a disagreement between MDI and the Company regarding the use of these accounts but these disputes were resolved by April 28, 1992. (Defendants Exhibit 6)

148. The monies in the special account were paid to AFSLIC within one to two weeks after deposited into the special account. (Tr 114)

149. No fees are paid to AMERICAN SERVICE. (Tr 1419)

150. No Missouri policyholders paid any monies into SERVICE. All Missouri policyholders pay all their premiums directly into AFSLIC's account. (Tr 397, 1440)

151. SERVICE is not an administration for AFSLIC under Section 375.425-929 R.S.Mo.

152. On June 24, 1992, AFSLIC wrote HOBBS requesting guidance regarding the filing of an audited

financial statement. The dilemma arose because of the confidentiality required under the Administrative Supervision Statute coupled with the insistence by the independent auditors that they must disclose the Supervision in their public audit. The assistance of the Supervisor was requested. (Defendant's Exhibit 17)

153. On June 26, 1992, HOBBS responded stating that "the decision of whether to file audited statements is one that the company must make". In that letter HOBBS discussed the action which various states, in which the company was admitted, excluding Missouri, might take. HOBBS failed to give the slightest indication that the MDI might take action. (Plaintiff's Exhibit 2)

154. MDI granted an extension of time to file the audited financial statement until August 3, 1992 but no statement was filed by that date. (Defendant's Exhibit 14 and Plaintiff's Exhibit 1.)

155. On September 21, 1992, HOBBS wrote a letter to OETTING with a copy to MELAHN discussing the actions that other states have taken regarding AFSLIC's failure to file an audited statement. There was no mention made of any demands by MDI for the audited statement, or any indication of potential actions by MDI. (Plaintiffs Exhibit 18)

156. MONACO requested another extension of the audit, however Plaintiff never responded. (Defendant's Exhibit 16)

157. Throughout the Supervision, HOBBS was aware of the conflict between the filing of the audited statement and the confidentiality requirement of the

Administrative Supervision, and had numerous discussions with the Company's independent auditors. HOBBS further received several draft copies of the audit. (Defendant's Exhibit 15, T-302, 303, 304, 305, 306, T-1262)

158. All information which would have been included in an audited financial statement have been presented to HOBBS through the draft of the audit. (Tr 1262, 304, Defendant's Exhibit 15)

159. Moreover, MDI examiners were on the premises throughout 1992, originally doing an exam as of December 31, 1991. The audit was used to verify the numbers on the company's statement. The examination accomplishes the same purpose; however, according to OETTING with greater independence. (Tr 1445, 1366)

160. AFSLIC cooperated fully with HOBBS and MDI with regard to supplying the audited financial statement and continued its attempt to supply such a statement.

161. Any further delay in producing an audited statement is caused by HOBBS agreeing to sign a letter of representation for the auditors and then refusing to do so. (Tr 310, 311 and 1264)

162. In Count VIII of Plaintiff's Petition For Rehabilitation MDI alleged that AFSLIC refused to release 1991 financial information on its non-insurance affiliates as it pertains to the insurer, and states that Defendant violated §374.190 RSMo.

163. The information which Plaintiff was seeking was information pertaining to SERVICE.

164. No monies belonging to AFSLIC were placed into an account in the name of SERVICE until January,

1992. Although there were alleged delays, all banks statements, reconciliations and cancelled checks regarding the 1992 accounts of SERVICE pertaining to AFSLIC were turned over to MDI. (Tr 314, 315, 445, 1387, 1388)

165. Marcotte, the examiner, found no irregularities in the financial information received. (Tr 1435)

166. There was no financial evidence that information of SERVICE in 1991 pertained to AFSLIC.

167. There was no evidence that any records pertaining to AFSLIC were not produced.

168. The evidence indicated that the company generally was cooperative when information or access was needed. (Tr 1028)

169. Evidence was offered that AFSLIC violated the ORDER of Supervision (Plaintiff's Exhibit 3) by issuing policies to six car dealers without approval. (Plaintiff's Exhibit 21)

170. The Order of Supervision only prohibits renewal of policies. (Plaintiff's Exhibit 3)

171. The Order of Supervision prohibits without approval any "new premiums." Such term is vague as all premiums received by AFSLIC in 1992 are new premiums and there was no evidence that there was any objection to the receipt of the same except as to excessive amount thereof.

Conclusions of Law

1. The certified copy of the report of financial examination submitted by the Plaintiff as Exhibit 1 is prima

facie evidence of the facts therein pertaining to the condition and affairs of Defendant as of September 30, 1992. Section 375.630.1(1) R.S.Mo.

2. The entry of the certified copy of the financial examination into evidence gives rise to a rebuttable presumption of the facts therein and it creates a rebuttable presumption that the facts therein are true as of the date of the hearing. Section 375.630.1(2) and (3).

3. Given the rebuttable presumption established by the entry of the certified copy of the financial examination into evidence, Defendant AFSLIC bears the burden of proof to rebut the Director's evidence as to the condition and affairs of AFSLIC.

4. The facts contained in the examination of AFSLIC by Plaintiff are pertinent only to the extent as they relate to specific allegations contained in Plaintiff's Petition For Rehabilitation.

5. Defendant has not met its burden of proof on each and every allegation and count set forth in the Verified Petition For Rehabilitation.

6. The regulation of insurance properly comes within the police power of the State.

7. The Missouri Insurance Code is a complete regulatory scheme, and courts are without authority to interfere with its administration by the Director of Insurance, the Plaintiff herein.

8. It is well-established that the Plaintiff is clothed with much discretion in regulating the business of insurance in Missouri.

9. The Plaintiff is statutorily directed to act in the best interest of, and to protect the general public, policyholders, insurance companies, and the officers, directors and shareholders thereof. Missouri Revised Statute Section 374.040(1).

10. Pursuant to this legislative directive, the Plaintiff has the power to supervise and regulate insurance companies which, in his view, require it.

11. This power to regulate includes the rehabilitation of insurers which the Plaintiff deems to be in such condition that the further transaction of business would be hazardous financially to the insurer's policyholders, creditors, or the public.

12. The Plaintiff is presumed to be acting faithfully in pursuit of the public interest absent evidence to the contrary.

13. Pursuant to Missouri Revised Statute section 374.045, the MDI has the power to promulgate rules and regulations to effectuate or aid in the interpretation of the insurance laws.

14. The Plaintiff is clothed with much discretion in regulating the business of insurance.

15. Action by the Plaintiff under Section 375.1165 R.S.Mo. is a discretionary action and not mandatory.

16. Equitable estoppel is generally not available against governmental bodies unless necessary to prevent manifest injustice.

Count I

17. In Count I of the Verified Petition, Plaintiff alleged that Defendant was in a hazardous condition because:

a. It has written premiums to its surplus at an excessive ratio or ratios, and

b. Plaintiff informed AMERICAN FINANCIAL of such excessive ratios "on more than one occasion" and the Defendant has not taken reasonable actions to reduce such ratios.

18. The ratio guideline of $3.00 of written premium to $1.00 of capital and surplus is not common to all types of companies and all types of written insurance.

19. AFSLIC ratio of written premiums to capital and surplus was excessive without the existence of reinsurance at all times that would offset any detrimental change in overall surplus as regards to policyholders.

20. AFSLIC did not take all reasonable actions available to it that were effective in reducing such ratios by infusion of capital, reduction of premiums or adequate reinsurance.

21. AFSLIC ratio of written premiums to capital and surplus is excessive and a condition that makes the further transaction of business hazardous to its policyholders, creditors or public, a ground for an order authorizing Plaintiff to rehabilitate Defendant AFSLIC under Section 375.1165(1) R.S.Mo.

Count II

22. In Count II of the verified Petition For Rehabilitation it is alleged that AFSLIC overstated its surplus by failing to "provide loss reserve credits which reflect the expected recoverable from its Lloyds reinsurer based upon the estimated amount of risks transferred."

23. AFSLIC's September 30, 1992 statement took reserve credits for the Lloyd's Treaty as though it covered the dates of January through September, 1992. The previous coverage dates were from April through December 1992. Although there were attempts to change the coverage dates the final Lloyd's Reinsurance Policy covered the April through December dates for 1992 as shown by Defendant's Exhibit 79. Defendant did not overcome the presumption that it overstated its surplus as regards policyholders as of September 30, 1992.

24. AFSLIC overcame the presumption that the methodology used in calculating basic reserve credits allowed under the Lloyds Treaty on September 30, 1992 were incorrect provided they complied with various rules and regulations promulgated by the MDI.

25. The Lloyd's Treaty would have been in conflict with MDI Regulation 20 C.S.R. 200-2.300(4)6 had it not received the prior approval of Plaintiff under 20 C.S.R. 200. – 2.300(4)(B).

26. Plaintiff's failure to advise Defendant of the ultimate disapproval of the methodology used under the Lloyds Treaty by Defendant until January, 1993 would be

manifestly unjust to Defendant not to allow such methodology on September 30, 1992 and Plaintiff is estopped from disapproving such methodology on that date.

27. AFSLIC overstated its reserve credits and resulting surplus and is in such a condition that the further transaction of business would be hazardous to its policyholders, creditors or the public, a ground for an order authorizing Plaintiff to rehabilitate Defendant AFSLIC under Section 375.1165(1) R.S.Mo.

Count III

28. Count III of the Verified Petition For Rehabilitation alleged that AFSLIC's admissible assets do not exceed its liabilities plus capital and surplus as required by law.

29. AFSLIC must have capital in an amount of $1,300,000 (the amount of its issued shares) and surplus of $600,000. The minimum capital and surplus by statute of $600,000 capital and $600,000 surplus. 376.280 R.S.Mo.

30. AFSLIC has not overcome the presumption of the facts set forth in Plaintiff's Exhibit 1 that its admissible assets are less than its liabilities plus capital and surplus as required by law and is in such a condition that the further transaction of business would be hazardous to its policyholders, creditor or the public, a ground for an order authorizing Plaintiff to rehabilitate Defendant AFSLIC under Section 375.1165(1) R.S.Mo.

Count IV

31. In Count IV of the Verified Petition For Rehabilitation, Plaintiff alleges Defendant AFSLIC violated the Order of Administrative Supervision or other valid order.

32. The facts recited in Count IV as being in violation of the Order of Administrative Supervision are not contained in such order but are attached thereto as a List of Requirements To Rescind Determination of Administrative Supervision or merely directives from MDI employees which are not a lawful order of the Plaintiff and are therefore are [sic] not grounds for an order of rehabilitation.

Count V

33. In Count V of the Verified Petition For Rehabilitation, Plaintiff alleged that AFSLIC did not file its Auditor's Financial Report on or before May 1, 1992.

34. AFSLIC did not willfully violate 375.1030 due to circumstances beyond its control and the inability of its auditor to obtain required information and cooperation of MDI personnel and such is in the exercise of sound discretion by Plaintiff not a ground for an Order of Rehabilitation. Section 375.1165 R.S.Mo. does not mandate the Plaintiff to seek rehabilitation under its provisions but is discretionary.

Count VI

35. In Count VI of the Verified Petition For Rehabilitation, Plaintiff alleges that the financial condition of

AFSLIC has deteriorated since the seizure. (January 7, 1993)

36. There being no evidence adduced in support of the allegations set forth in Count VI the same found against the Plaintiff and in favor of Defendant AFSLIC.

Count VII

37. Count VII of Plaintiff's Verified Petition For Rehabilitation alleges AFSLIC willfully violated § 375.925.2 R.S.Mo.

38. No evidence was adduced that AFSLIC collected charges, premiums from or adjusted or settled claims of residents of Missouri or was in violation of § 375.925 R.S.Mo.

39. Count VII is found in favor of Defendant AFSLIC and against Plaintiff.

Count VIII

40. Count VIII of Plaintiff's Verified Petition For Rehabilitation alleges AFSLIC failed to make available for examination the book accounts and records of any subsidiary or related company so far as they pertain to AFSLIC.

41. No evidence was adduced that any books, accounts and records of affiliated companies contained any information relating to the affairs of AFSLIC other than those books, accounts and records that were in fact produced.

42. Count VIII is found in favor of Defendant AFSLIC against Plaintiff.

Respectfully submitted,

/s/ James P. Dalton
James P. Dalton, Special Master

IN THE CIRCUIT COURT OF COLE COUNTY
STATE OF MISSOURI

JAY ANGOFF, Director, Department of Insurance State of Missouri,	)	
Plaintiff,	)	Case No. CV193-107CC
v.	)	
AMERICAN FINANCIAL SECURITY LIFE INSURANCE COMPANY,	)	
Defendant.	)	

ORDER OF REHABILITATION

This matter comes before the court on the verified Petition for Rehabilitation filed by the Director of the Department of Insurance of Missouri against the defendant American Financial Security Life Insurance Company. The Court referred this matter pursuant to Supreme Court Rule 68.01 and Section 375.610 R.S.Mo. by Order of Reference to James Dalton to act as Special Master. The trial of this matter was before Special Master James Dalton. The Special Master's Report to the Court was filed on March 11, 1993 and contained Findings of Fact and Conclusions of Law.

Plaintiff filed his Motion for Entry of Order of Rehabilitation and Objections to Some Portions of Special Master's Report to the Court and defendant filed Exceptions to the Report of the Special Master and those matters were heard by the Court on March 18, 1993.

This Court has reviewed the Report of Special Master and has reviewed the motions and objections filed by the parties hereto; and being duly advised in the premises the Court hereby adopts the Special Master's Report to the Court and its Findings of Fact and Conclusions of Law pursuant to Rule 68.01(g)(3) of the Missouri Rules of Procedure.

The Court finds that plaintiff has proved grounds sufficient to place defendant AFSLIC into rehabilitation pursuant to Section 375.1165 R.S.Mo. because AFSLIC is operating in hazardous condition.

NOW, THEREFORE, IT IS ORDERED, ADJUDGED AND DECREED that:

1. Jay Angoff, Director of the Department of Insurance of the State of Missouri, or his successors, is authorized to rehabilitate American Financial Security Life Insurance Company ("AFSLIC"); and

2. The Director is appointed as rehabilitator of AFSLIC; and

3. The Director as rehabilitator shall forthwith take possession and control of all assets, real property, personal property, books, accounts, records, documents and papers of the defendant and of the premises occupied by defendant for transaction of its business; and

4. Rehabilitator shall receive and collect all premium and other income due to defendant; and

5. Title to all assets of the insurer shall vest in the Director as rehabilitator of AFSLIC; and

6. Rehabilitator shall file written accountings with this Court every six months following this Order until further order of the Court; and

7. Each accounting shall include a report concerning the rehabilitator's opinion as to the likelihood that a plan will be prepared under Section 375.1168(4) with a time-table for doing so; and

8. The Director as rehabilitator may appoint one. or more special deputies, who shall have all the powers and responsibilities of the rehabilitator granted under this section, and the Director may employ such counsel, clerks and assistants as the Director deems necessary. The compensation of the special deputy, counsel, clerks and assistants and all expenses of taking possession of the insurer shall be fixed by the Director with the approval of the Court and shall be paid out of the funds or assets of the insurer; and

9. The authority of all directors, officers, and managers of defendant is hereby suspended and their powers are vested in the rehabilitator, except as such powers are re-delegated by the rehabilitator; and

10. The rehabilitator shall have full power to direct and manage the defendant company; to collect premiums and administer claims; to sell property of defendant; to collect accounts receivable and to pay accounts payable as he deems fit; to terminate or affirm contracts, agreements and/or leases; to have and discharge employees subject to contract rights, if any; and to deal in all manner with the property and business of defendant; and

11. The rehabilitator may pursue all legal remedies on behalf of the defendant; and

12. The rehabilitator shall have all powers provided by law to avoid fraudulent transfers; and

13. This Order shall operate to stay any pending lawsuit, action or legal proceeding in any court in this state wherein the defendant insurer is a party or is obligated to defend as a party for ninety days after the date herein, and for such additional time as rehabilitator requires; and

14. Rehabilitator shall take such action respecting pending litigation as he deems necessary in the interests of justice and for the protection of creditors, policyholders and the public and may settle, compromise, dismiss or try or otherwise dispose of said matters as he deems prudent; and

15. The rehabilitator shall consider all litigation pending outside the state and shall petition the courts with jurisdiction over said matters for a stay of litigation when he deems it necessary to protect the estate of insurer; and

16. Defendant AFSLIC and its officers, directors, managers, agents and employees are enjoined from disposition of its property and from the transaction of any of its business except as directed in writing by plaintiff.

/s/ Thomas J. Brown
Judge Thomas Brown

Ordered this 30th day of March, 1993.

UNITED STATES COURT OF APPEALS
FOR THE EIGHTH CIRCUIT

No. 93-4083WMJC

Thomas A. Warmus,
Appellant,

vs.

Lewis Melahn, et al. ,
Appellees.

Order Denying Petition for Rehearing and Suggestion for Rehearing En Banc

The suggestion for rehearing en banc is denied. The petition for rehearing by the panel is also denied.

September 21, 1995

Order Entered at the Direction of the Court:

/s/ Michael E. Gins

Clerk, U.S. Court of Appeals, Eighth Circuit

UNITED STATES DISTRICT COURT FOR THE
WESTERN DISTRICT OF MISSOURI

THOMAS A. WARMUS

Plaintiff,

vs.

CASE NO.:
93 4306-CV-C-5

LEWIS MELAHN, JAMES OETTING and WILLIAM HOBBS, III

Defendants.

_____ /

COMPLAINT AND DEMAND FOR JURY TRIAL

(Filed Jul. 6, 1993)

COMES NOW, Plaintiff, THOMAS A. WARMUS, by and through his undersigned counsel, and files his Complaint against Defendants, LEWIS MELAHN, JAMES OETTING, and WILLIAM R. HOBBS, III, and allege as follows:

JURISDICTION – VENUE

1. Jurisdiction of the federal court exists pursuant to 28 USC, §1331 since this is a civil action arising under the laws and constitution of the United States of America. This action involves a violation of federal law pursuant to 42 USC §1983.

2. Jurisdiction of the federal court also exists pursuant to 28 USC §1343, since this is a civil action between citizens of different states.

3. The amount in controversy exceeds fifty thousand dollars ($50,000) exclusive of interest and costs.

4. Plaintiff further invokes supplemental jurisdiction of this court to hear and decide claims arising under state law.

5. Venue is proper in this district since the cause of action alleged in this Complaint occurred in Cole County, Missouri which is located in said district.

6. Plaintiff, THOMAS A. WARMUS (WARMUS) is a citizen of the United States, a resident of the State of Florida and the beneficial owner, president and director of AMERICAN FINANCIAL SECURITY LIFE INSURANCE COMPANY (AMERICAN FINANCIAL) and AMERICAN WAY HOLDING, INC. (HOLDING).

7. HOLDING, not a party to this action, is a corporation organized and existing under the laws of the State of Florida with its principal place of business in Broward County, Florida with no offices in the State of Missouri, and the one hundred percent stockholder of AMERICAN FINANCIAL.

8. AMERICAN FINANCIAL, not a party to this action, is an insurance company organized under the laws of the State of Missouri, as a life insurer, writing credit life and disability insurance. AMERICAN FINANCIAL was placed into Rehabilitation by the Circuit Court of Cole County, Missouri on March 30, 1993. Said Order is currently being appealed.

9. Defendant, LEWIS MELAHN, (MELAHN) was the Director of the Missouri Department of Insurance (MDI) at all times pertinent to the allegations of this

Complaint, including the time between the filing of the Administrative Supervision against AMERICAN FINANCIAL and the filing of an action seeking Rehabilitation of AMERICAN FINANCIAL.

10. MELAHN is a resident of the State of Missouri and is being sued in his individual capacity.

11. Defendant, JAMES OETTING, (OETTING) was the Chief Financial Examiner of the MDI at all times pertinent to the allegation of this Complaint including the time between the filing of the Administrative Supervision against AMERICAN FINANCIAL and the filing of an Action in Seizure against AMERICAN FINANCIAL.

12. OETTING is a resident of the State of Missouri and is being sued in his individual capacity.

13. Defendant WILLIAM R. HOBBS, III (HOBBS) was the Administrative Supervisor of AMERICAN FINANCIAL from May 4, 1992, until the end of Administrative Supervision, representative of MELAHN during Seizure, and at the time this Complaint was filed, Deputy Rehabilitator of AMERICAN FINANCIAL.

14. HOBBS is a resident of the State of Kansas and is being sued in his individual capacity.

15. At all times relevant to the allegations of this Complaint and in all actions of the Defendant, MELAHN, HOBBS and OETTING, alleged herein, all Defendants were acting under color of law under the authority of MDI.

GENERAL ALLEGATIONS TO ALL COUNTS

16. WARMUS has been a licensed insurance agent and broker since 1958, and for more than thirty years has specialized in the sale of credit life and disability policies through agents affiliated with automobile dealers to purchasers of financed motor vehicles.

17. WARMUS owns and controls a holding company system made up of seven insurance companies and three non-insurance companies that primarily service his credit insurance business.

18. On May 2, 1989, WARMUS, through HOLDING, purchased the insurance company that became known later that month as AMERICAN FINANCIAL.

19. AMERICAN FINANCIAL is a member of a holding company system beneficially owned and controlled by WARMUS which holding company system includes an insurance company located in Michigan named AMERICAN WAY LIFE INSURANCE COMPANY (LIFE).

20. In 1989 WARMUS discussed with MDI, that he and his companies had been unfairly discriminated against by the Michigan Insurance Bureau for years, that WARMUS had plans to streamline his holding company system, move the credit life and disability insurance of LIFE to AMERICAN FINANCIAL and make AMERICAN FINANCIAL the "flagship" or principal provider of the WARMUS credit insurance business.

21. The bulk of the credit insurance customers serviced by LIFE and then by AMERICAN FINANCIAL are located in the State of Michigan.

22. AMERICAN FINANCIAL began receiving premiums from Michigan residents in January 1992, after its policies, premiums and agency contracts were approved by the appropriate regulatory authorities.

23. Prior to January 1992, the agents responsible for the credit life business had sold the credit insurance policies of LIFE.

24. This book of business had been developed by WARMUS, in over thirty years in the industry in which WARMUS had developed a good solid relationship with the agents and an excellent reputation in the industry.

25. The transfer of business from LIFE to AMERICAN FINANCIAL was part of a long-range plan which was previously discussed with the MDI in 1989; however, the actual transfer date was accelerated by regulatory action taken by the Michigan Insurance Bureau against LIFE.

26. In early 1992, Defendants, MELAHN and OETTING, joined in a conspiracy with officials of the Michigan Insurance Bureau which had as its purposes the liquidation of AMERICAN FINANCIAL, the elimination of WARMUS from the insurance industry, and the destruction of the relationship WARMUS had created with various automobile dealers and their insurance agencies.

27. To effect that conspiracy, MELAHN and OETTING sent a team of financial examiners to the headquarters of AMERICAN FINANCIAL in Southfield, Michigan. The stated purpose of the examination was to ascertain the financial condition of AMERICAN FINANCIAL as of

December 1991, but the true purpose was to burden AMERICAN FINANCIAL with the costs of the examination, which it was legally required to bear and to discover some arguable basis to take control of AMERICAN FINANCIAL, destroy the company and drive THOMAS WARMUS out of the insurance industry. Although the examiners examined the books and records of AMERICAN FINANCIAL continuously from February through July 1992, no examination report was ever produced for the period examined.

28. Shortly after burdening AMERICAN FINANCIAL with the costs of the unnecessary financial examination, on March 6, 1992, Defendants, MELAHN and OETTING, took an additional step to carry out the conspiracy to force WARMUS out of the insurance business by placing AMERICAN FINANCIAL in Administrative Supervision. The Supervision was legally unjustified, and was undertaken to burden AMERICAN FINANCIAL with another layer of unnecessary expense and to enmesh its operation in cumbersome administrative regulations. Pursuant to state statutes §375.1160.4 RSMo and orders of MELAHN, virtually any actions taken in the continuing operations of AMERICAN FINANCIAL after the Order of Administrative Supervision required the prior approval of the Director of Insurance or his appointed supervisor. As a result, AMERICAN FINANCIAL has been under the complete control and dominion of Defendants.

29. MELAHN and/or OETTING placed conditions on AMERICAN FINANCIAL, which they required to be completed prior to the termination of the Supervision, which conditions were unrealistic, impossible to meet, and without any valid justifiable basis.

30. Originally, MELAHN appointed JOSEPH FINK (FINK) as Administrative Supervisor of AMERICAN FINANCIAL.

31. On May 4, 1992, Plaintiff extended the Order of Administrative Supervision and appointed HOBBS to replace FINK as Administrative Supervisor of AMERICAN FINANCIAL.

32. Defendant, HOBBS, was brought into conspiracy when he was hired by Defendant, MELAHN, to serve as Administrative Supervisor of AMERICAN FINANCIAL. Whether HOBBS understood the goals of the conspiracy when he was initially hired for this position is presently unknown, but he learned of them and ratified the unlawful enterprise and joined the conspiracy shortly after being appointed as Administrative Supervisor.

33. HOBBS remained in his capacity as Administrative Supervisor of AMERICAN FINANCIAL throughout the supervision which terminated on January 7, 1993 when AMERICAN FINANCIAL was served with an ex parte seizure order for the Circuit Court of the State of Missouri in Cole County, Missouri obtained by MELAHN as Director of the MDI, seizing AMERICAN FINANCIAL's assets and enjoining it from further conducting its business except with Plaintiff's written consent.

34. AMERICAN FINANCIAL filed a timely challenge to the *ex parte* seizure order with the Court; however, before the Court could resolve that challenge, MELAHN mooted that case by filing a Petition For Rehabilitation against AMERICAN FINANCIAL in the same Court on February 1, 1993, in retaliation for AMERICAN

FINANCIAL seeking a judicial review of Melahn's actions in that case.

35. During the period of Administrative Supervision, AMERICAN FINANCIAL was ordered not [sic] enter into reinsurance contracts without the approval of MELAHN or his appointed supervisor, HOBBS, who was specifically delegated that authority by order of MELAHN.

36. During the Administrative Supervision, the most important issue became reinsurance since such reinsurance would allow AMERICAN FINANCIAL to maintain its volume of premiums written, as well as resolve the initial surplus strain on AMERICAN FINANCIAL, resulting from the type of business sold and the statutory accounting procedures required for insurance companies.

37. Continuously since the outset of their participation in the conspiracy, MELAHN and OETTING claimed that the volume of premiums written by AMERICAN FINANCIAL was excessive in relation to its capital and surplus and demanded that AMERICAN FINANCIAL take steps to reduce that volume. AMERICAN FINANCIAL attempted to meet that demand by obtaining reinsurance satisfactory to Defendants, which reinsurance would permit AMERICAN FINANCIAL to write at premium volume acceptable to Defendants. However, Defendants continuously refused to approve reasonable reinsurance treaties or have repudiated approvals that they provided to AMERICAN FINANCIAL and WARMUS unreasonably and for the sole purpose of continuing the conspiracy to deprive WARMUS of his civil right to engage in the business of insurance.

38. AMERICAN FINANCIAL in June 1992 was offered reinsurance from LLOYD's of London (LLOYDS) for all of the business it wrote or would write during the last nine months of 1992.

39. In June 1992, AMERICAN FINANCIAL presented the LLOYDS reinsurance treaty to HOBBS for regulatory approval.

40. The central, if not the sole issue in determining whether to approve the LLOYD'S treaty, was the accounting methodology which determined the appropriate amount of reserve credits that AMERICAN FINANCIAL, as the ceding insurer, would be permitted to take on its balance sheet.

41. On or about June 24, 1992, AMERICAN FINANCIAL sent HOBBS projections concerning the LLOYD's treaty, which projections included the amounts of premiums expected to be written during the remainder of 1992 and the amounts of reserve credits which the company expected to receive. The projections were based upon the assumptions that AMERICAN FINANCIAL would be writing two million five hundred [sic] dollars ($2,500,000) per month in premiums in 1992 under the Administrative Supervision and that the reserve credits which AMERICAN FINANCIAL would receive for nine months of coverage would be approximately nine million dollars ($9,000,000).

42. On June 26, 1992, HOBBS requested of AMERICAN FINANCIAL that he receive a copy of the proposed treaty with LLOYDS, a description of the method for calculating reserve credits, and projected financial impact for 1992 and 1993.

43. Additionally, on June 26, 1992, HOBBS advised AMERICAN FINANCIAL that prior to approval of the reinsurance treaty, it was necessary to obtain an independent actuarial opinion with regard to "reserve calculation and proposed statutory reinsurance credits.

44. AMERICAN FINANCIAL complied with all requests of HOBBS including the request for an independent actuarial opinion, even though the accounting methodology had been already established and reviewed by an actuary who was an expert in the credit life disability field and who was intimately familiar with the WARMUS book of business.

45. HOBBS chose as his independent actuary, SAM GUTTERMAN (GUTTERMAN) from the firm of PRICE WATERHOUSE, to review the accounting methodology of the proposed treaty with LLOYDS and to ascertain if there was a transfer of risk. GUTTERMAN, in his evaluation of the proposed LLOYDS reinsurance treaty and its accounting methodology, found that there was transfer of risk and that the reserve methodology was correct given a few minor adjustments.

46. AMERICAN FINANCIAL made those adjustments suggested by GUTTERMAN.

47. On July 20, 1992, HOBBS wrote OETTING, with a copy of said letter sent to MELAHN, in which HOBBS explained the terms of the reinsurance treaty with LLOYDS and advised both OETTING and MELAHN that he intended to approve the treaty with LLOYDS. HOBBS attached a copy of the proposed reinsurance treaty with LLOYD's to the correspondence to OETTING and MELAHN.

48. On August 3, 1992, with the knowledge and the consent of MELAHN and OETTING, HOBBS approved the reinsurance treaty between AMERICAN FINANCIAL and LLOYDS and its accounting methodology and within several days thereafter, advised both OETTING and MELAHN of this approval.

49. The LLOYD's reinsurance treaty, as approved by MELAHN, OETTING and HOBBS in August 1992 covered the last nine months of 1992.

50. By August 5, 1992 at the latest, HOBBS advised OETTING and MELAHN of the amount of premiums expected to be written by AMERICAN FINANCIAL by the end of the year, as well as the amount of reinsurance credits which would be taken for nine months of the reinsurance treaty with LLOYDS.

51. MELAHN, OETTING and HOBBS did not advise AMERICAN FINANCIAL or WARMUS at any time during 1992 that there was any doubt regarding the accounting methodology for the LLOYD's treaty or the amount of available reinsurance credits for the nine months of 1992, which accounting methodology and reserve credit had been approved both orally and in writing by HOBBS with the full knowledge and consent of MELAHN and OETTING.

52. The first time WARMUS or FINANCIAL discovered that HOBBS, MELAHN and OETTING reversed their approval regarding the accounting methodology on reserve credits for the LLOYD's treaty was on January 6, 1993, when AMERICAN FINANCIAL was served with an exparte Seizure Order.

53. By August 11, 1992, HOBBS with the consent of MELAHN and OETTING authorized payment by AMERICAN FINANCIAL of the initial deposit premium to the LLOYDS broker, which initial deposit premium was in excess of two hundred thousand dollars ($200,000).

54. Throughout 1992, HOBBS, OETTING and MELAHN misled WARMUS and AMERICAN FINANCIAL into believing the MDI approved the accounting methodology and reserve credits for the LLOYD's treaty.

55. By late August or early September, 1992, ROBERT BAILEY, (BAILEY) the Deputy Commissioner of the Michigan Insurance Bureau, advised HOBBS, MELAHN and/or OETTING that he did not agree with the accounting methodology for the LLOYD's treaty, and HOBBS, MELAHN and OETTING decided, in conspiracy with BAILEY to disapprove the credits, keep the disapproval of the credits secret until after an examination was complete, and drive WARMUS and AMERICAN FINANCIAL out of the insurance business.

56. The Michigan Insurance Bureau has been unjustifiably affecting WARMUS, for over thirteen years and personnel from the Michigan Insurance Department, as well as personnel from the MDI including, without limitation, MELAHN, HOBBS and OETTING, conspired to put WARMUS out of the insurance business by destroying the valuable book of business owned and developed by WARMUS and destroying AMERICAN FINANCIAL.

57. By September 1992, OETTING, in his capacity of Chief Financial Examiner of the MDI, decided that the company should receive no credits whatsoever for the

reinsurance treaty with LLOYDS and communicated his decision to both HOBBS and MELAHN.

58. Although by September of 1992 MELAHN, OETTING and HOBBS knew that they would reserve their approval of the accounting methodology for the LLOYD's reinsurance treaty in the amount which was also previously approved by them and which was also approved by the independent actuary chosen by HOBBS, as well as two other actuaries, and that without the reserve credits taken pursuant to the accounting methodology, AMERICAN FINANCIAL would be statutorily insolvent, and writing at a level at which the ratios of premium to surplus would not be acceptable without reinsurance, HOBBS, MELAHN and OETTING did not advise WARMUS or AMERICAN FINANCIAL of this disapproval, but deceived WARMUS and AMERICAN FINANCIAL into believing that there was no question as to the appropriate accounting methodology or amount of allowable reserve credits on the LLOYDS reinsurance treaty.

59. The actions by HOBBS, MELAHN and OETTING in initially approving the reinsurance treaty about LLODYS [sic] and in keeping silent about their subsequent reversal of their decision regarding the accounting methodology, were intentionally designed to deceive and mislead WARMUS and AMERICAN FINANCIAL into a false sense of security, and designed to deceive WARMUS and AMERICAN FINANCIAL into believing that the reinsurance credits were acceptable so as to prevent AMERICAN FINANCIAL or WARMUS from taking other steps to secure a different type of reinsurance treaty or to correct the concerns of MDI.

60. The reliance of WARMUS and AMERICAN FINANCIAL on the written as well as verbal representations of HOBBS in his capacity as the Administrative Supervisor of AMERICAN FINANCIAL, was reasonable, especially given the nature of the Administrative Supervision and the high degree of control that MELAHN, OETTING and HOBBS had over the affairs of AMERICAN FINANCIAL. Moreover, as the purpose of an Administrative Supervision was to correct any concerns with the insurer, the reliance upon advice of officials of the MDI and its appointed representatives by WARMUS and AMERICAN FINANCIAL was exceptionally reasonable.

61. After the written approval of the LLOYDS reinsurance credits by HOBBS, and after MELAHN, HOBBS and OETTING decided to disallow said credits, MELAHN caused a financial exam of AMERICAN FINANCIAL to be performed, examining the financial condition of AMERICAN FINANCIAL as of September 30, 1992, in an attempt to exploit a timing issue of changes approved by HOBBS in late 1992.

62. Although AMERICAN FINANCIAL had not been advised by HOBBS, OETTING, MELAHN or anyone else at the MDI that there was any question regarding the accounting methodology for the reinsurance credits with the LLOYD's treaty, this accounting methodology became a central focus of the financial exam.

63. HOBBS and other employees at MDI at the direction of MELAHN or OETTING, attempted to persuade the independent actuary appointed by HOBBS to

change his opinion regarding the accounting methodology for the LLOYDS reinsurance treaty, but in spite of the pressure by MDI, said actuary refused to change his opinion.

64. In order to declare AMERICAN FINANCIAL insolvent, OETTING caused the financial examiner in charge of the examination of AMERICAN FINANCIAL to have MDI's own in-house actuary give his opinion.

65. MDI's in-house actuary recommended that further questions be asked regarding the accounting methodology of the actuaries who previously approved the same; however, despite this suggestion from their own actuary, MELAHN and OETTING refused and failed to contact the other actuaries but rather caused an examination report to be filed giving eight hundred thousand dollars ($800,000) credit for the reinsurance treaty, instead of the in excess of eight million dollars ($8,000,000) which was previously approved.

66. Due to the disallowance of over seven million dollars ($7,000,000) of previously approved reinsurance credits, MDI fraudulently alleged that AMERICAN FINANCIAL was statutorily financially impaired on said examination report as of September 30, 1992.

67. Although it is customary in Missouri to have an exit conference between the examiners and the company prior to the examination report being filed to discuss and attempt to resolve the differences between the financial examiner and the insurer, at the direction of OETTING and/or MELAHN, no exit conference was in fact scheduled. This resulted in the financial examination being concluded and a final examination report being written

without anyone from MDI advising the company that there was a reversal of approval regarding the reinsurance credits with LLOYDS, leading the company to believe that the reinsurance credits remained approved. This effectively prevented AMERICAN FINANCIAL and WARMUS from taking other steps necessary to protect its property rights.

68. Had HOBBS, MELAHN or OETTING timely questioned or disapproved the reinsurance treaty with LLOYDS, AMERICAN FINANCIAL could have obtained other reinsurance to meet Defendants' complaints about the relationship between its premiums and its capital and surplus. Defendants disapproved of this treaty after the fact solely to enable them to seize AMERICAN FINANCIAL and assist the conspiracy to deprive WARMUS of his civil right to engage in the business of insurance.

69. Defendants had no legal basis for barring AMERICAN FINANCIAL from taking credit for its reinsurance treaty with LLOYDS. Their objections to the treaty were rejected by the Special Master and Circuit Court Judge who ruled upon the Petition For Rehabilitation. In addition, when the MDI was given control over AMERICAN FINANCIAL in rehabilitation after MELAHN and OETTING left office, their successors with the continued connivance of HOBBS have continued to pay the remaining premiums due for the LLOYDS policy.

70. In August 1992, when AMERICAN FINANCIAL secured the reinsurance treaty with LLOYDS, the initial coverage period of the reinsurance treaty was the last nine months of 1992 because AMERICAN FINANCIAL had a reinsurance treaty with an affiliated insurer,

AMERICAN TREND (TREND), covering the first three months of 1992.

71. TREND was a member of the holding company system controlled by WARMUS and was licensed as an insurer by the State of Arizona.

72. WARMUS and AMERICAN FINANCIAL believed, based upon representations made in correspondence sent from MELAHN, that because of recent revisions in Missouri statutes regarding reinsurance that unauthorized carriers such as TREND would be acceptable reinsurers for financial statements filed with the Department of Insurance for the first three-quarters of 1992 without special trust accounts, but would not be acceptable on the financial statement as of December 31, 1992 and on all subsequent statements, without assets in trust.

73. AMERICAN FINANCIAL, on its June 1992 quarterly used credits from the reinsurance treaty with TREND for the first three months and from the reinsurance credits with LLOYDS for the next three months. On its September quarterly, AMERICAN FINANCIAL intended to use the reinsurance credits with TREND for the first three months and the reinsurance credits with LLOYDS for the next six months.

74. Although HOBBS, MELAHN and OETTING had known about TREND's reinsurance treaty with AMERICAN FINANCIAL since May 1992, until October 21, 1992, HOBBS, OETTING and MELAHN did not object to AMERICAN FINANCIAL receiving credits on its balance sheets for reinsurance ceded to TREND, as reflected on its June Quarterly Statement filed with the MDI and on its

proposed September Quarterly Statement which was given to HOBBS. To the contrary, in August when HOBBS was attempting to project the future financial condition of AMERICAN FINANCIAL for the benefit of HOBBS and OETTING, HOBBS made his calculations using the reinsurance credits for the TREND treaty for the first three months of 1992.

75. On October 21, 1992, long after AMERICAN FINANCIAL prepared and filed its June Statement, HOBBS reversed his prior position and advised AMERICAN FINANCIAL for the first time, that he disapproved of the taking of reinsurance credits for the treaty between AMERICAN FINANCIAL and TREND on the June, 1992 quarterly statement.

76. Even though HOBBS' request was untimely and unreasonable, and AMERICAN FINANCIAL had the right to use TREND and receive credits on its balance sheets until December 31, 1992, and thereafter with trusted assets, AMERICAN FINANCIAL in an attempt to placate MDI, complied with the mandate by its Administrative Supervisor HOBBS, and agreed not to use the credits from TREND on its September quarterly statement, provided that AMERICAN FINANCIAL obtained the consent of HOBBS and LLOYDS to revise the reinsurance coverage periods with LLOYDS from the last nine months of 1992 to the first nine months of 1992, that these changes would be reflected on the September quarterly, and that AMERICAN FINANCIAL would obtain insurance from another reinsurer for the last quarter of 1992.

77. There was no valid reason for HOBBS to reverse his position of TREND on the September quarterly, but said disallowance of TREND, was intended to drive AMERICAN FINANCIAL out of business, damage WARMUS and destroy his book of business.

78. In November, 1992 and again in December, 1992, AMERICAN FINANCIAL wrote HOBBS requesting formal approval for the revisions in the LLOYDS treaty and that these revisions in LLOYDS and the cancellation with TREND would be reflected on the September quarterly.

79. HOBBS, with the consent and knowledge of OETTING and MELAHN, approved the revision to the LLOYDS treaty to cover the first nine months of 1992 and failed to make any objections to its inclusion in the financial statement as of September 30, 1992.

80. The actions of MELAHN, HOBBS and OETTING deceived and misled WARMUS, HOLDING and AMERICAN FINANCIAL to attempt to cause them to weaken their statutory financial condition and destroy the company in furtherance with the conspiracy with the Michigan Insurance Bureau, notwithstanding on a generally accepted accounting principle basis, the company was and always remained solvent and profitable.

81. HOBBS, MELAHN and OETTING further deceived the company regarding reinsurance for the last quarter of 1992.

82. AMERICAN FINANCIAL required reinsurance for the last quarter of 1992 to replace the gap which was created when the LLOYDS treaty was revised from the last nine months of 1992 to the first nine months of 1992,

which revision was caused at the direction of HOBBS, MELAHN and OETTING.

83. During November and December of 1992, AMERICAN FINANCIAL discussed several proposed reinsurance treaties with difference [sic] reinsurers with HOBBS and eventually both HOBBS and AMERICAN FINANCIAL determined that the reinsurance with NRG AMERICA (NRG) would be acceptable.

84. HOBBS initially orally indicated his approval of the treaty with NRG during numerous discussions with AMERICAN FINANCIAL during the last quarter of 1992, and AMERICAN FINANCIAL presented an executed copy of the treaty with NRG at year's end requesting HOBBS' approval. Based upon prior discussions, AMERICAN FINANCIAL reasonably believed that HOBBS' approval had already been obtained.

85. In 1993, HOBBS without prior warning and at the direction or with the approval of MELAHN and OETTING reversed his position and refused to approve the treaty with NRG.

86. HOBBS reversed MDI's position on the NRG treaty and refused to allow the company to enter such treaty, even though such refusal would mean that the company would be financially statutorily impaired at year's end, without additional surplus relief.

87. The reversal of HOBBS positions of the NRG treaty was without any justification whatsoever.

88. HOBBS, MELAHN and OETTING refused to allow AMERICAN FINANCIAL to enter into a reinsurance treaty for the last quarter of 1992 to cause AMERICAN FINANCIAL to be statutorily impaired, which would allow MDI to place AMERICAN FINANCIAL in liquidation or rehabilitation destroying the company, as well as WARMUS book of business and reputation; thus, completing their conspiracy with Michigan Insurance Bureau.

89. By wrongfully and deliberately rejecting the proper reinsurance treaties that AMERICAN FINANCIAL negotiated with TREND, LLOYDS and NRG, Defendants enabled MDI's financial examiners to issue an examination report that falsely claimed that AMERICAN FINANCIAL was statutorily insolvent as of September 30, 1992. Defendants then presented that intentionally misleading report to the Circuit Court of Cole County as the primary justification for a petition to take control of AMERICAN FINANCIAL away from WARMUS and place it under the control of the MDI for purported rehabilitation. Defendants well knew that there was no true basis for placing AMERICAN FINANCIAL into rehabilitation, and that the rehabilitation would reduce or eliminate the value of AMERICAN FINANCIAL, destroy the long standing relationship between WARMUS and the agents which sold his insurance, and would make it difficult or impossible for WARMUS to remain in the business of insurance.

90. MELAHN, OETTING and HOBBS also knew that by placing the company in rehabilitation, that MDI would be given control of AMERICAN FINANCIAL, and

once under MDI's control, they would proceed to liquidate AMERICAN FINANCIAL and ruin THOMAS WARMUS.

91. Throughout the Administrative Supervision, HOBBS, MELAHN and OETTING led AMERICAN FINANCIAL and WARMUS to believe that it was appropriate for AMERICAN FINANCIAL to write 2.5 million dollars in premium per month before reinsurance.

92. HOBBS, OETTING and MELAHN made these representations regarding the 2.5 million dollars per month knowing that said representations were false when made, and that MDI subsequently would reverse its position, and unrealistically insist that any writings exceeding 1.4 million dollars per month would be hazardous. Said representations were meant to deceive and mislead WARMUS and AMERICAN FINANCIAL and to give MELAHN another justification to file for rehabilitation and eventually liquidation.

93. Missouri Statutes require that an insurance company, such as AMERICAN FINANCIAL, file audited financial statements; however, the company could not file such a statement in 1992 without violating the confidentiality requirements of Administrative Supervision.

94. HOBBS, MELAHN and OETTING caused WARMUS and AMERICAN FINANCIAL to believe that the only reason to file the audited financial statement would be to avoid problems with other states in which the company was licensed, and that the failure to file would not jeopardize the company's status or license in

Missouri. At no time, did HOBBS, MELAHN and OETTING advised [sic] Plaintiff that MDI would seek rehabilitation or liquidation if the audited financial statement was not timely filed.

95. HOBBS, MELAHN and OETTING made or allowed these representations to be made, intending to file an action for rehabilitation or otherwise against AMERICAN FINANCIAL for not timely filing its audited financial statement.

96. The actions of MELAHN, HOBBS and OETTING during the period of Administrative Supervision were intended to mislead Plaintiff and prevent him from taking the steps necessary to meet the requirements of MDI.

97. The actions and representations above stated by HOBBS, MELAHN and OETTING, under color of law prevented Plaintiff from taking the steps necessary to meet the requirements of the Missouri Statutes.

98. On January 6, 1993, MELAHN as Director of MDI filed a Verified Petition For A Seizure of AMERICAN FINANCIAL.

99. On January 7, 1993, MDI released its examination report of AMERICAN FINANCIAL which found the company to be statutorily insolvent because of the disallowance of the reinsurance credits on the treaty with LLOYDS which had been approved by MELAHN, OETTING and HOBBS. The company learned for the first time when it received the financial exam and the Petition For Seizure, that there was any question whatsoever by MDI regarding the amount of reinsurance credits or the reserve methodology.

100. On February 1, 1993, MELAHN, as Director of MDI filed a Petition For Rehabilitation and alleged the statutory insolvency of the company based primarily upon the disallowance of the reinsurance credits from the treaty with LLOYDS, that the company was writing premiums which were excessive in regards to its surplus as the premium writings were in excess of 1.4 million dollars per month, that it did not timely file its 1992 audited financial statement, and for a lack of cooperation with MDI in supplying records.

101. After a lengthy trial before a Special Master, the Special Master found in favor of AMERICAN FINANCIAL on five counts of eight counts, approved the accounting methodology for the LLOYDS treaty but did not allow AMERICAN FINANCIAL to receive credit for the full nine months of the LLOYDS treaty as of September 30, 1992, as the revisions in coverage with LLOYDS were not in place as of that date, and because of subsequent revisions made to the LLOYDS treaty in 1993, caused by MDI's refusal to approve a reinsurance treaty with NRG for the fourth quarter of 1992. The Special Master allowed AMERICAN FINANCIAL to receive credits for the LLOYDS treaty as of September 30, 1992, for six months instead of nine months. The finding against AMERICAN FINANCIAL on the three remaining counts of the Petition For Rehabilitation was due solely to AMERICAN FINANCIAL and WARMUS' compliance with the directions of their Administrative Supervisor, HOBBS, which directions were made with knowledge and approval of MELAHN and OETTING.

102. The court entered judgment affirming all findings of the Special Master and placed AMERICAN

FINANCIAL into rehabilitation on March 30, 1993 transferring all assets of AMERICAN FINANCIAL to the Director of MDI.

103. AMERICAN FINANCIAL appealed and MDI cross-appealed. MDI's cross-appeal was dismissed. AMERICAN FINANCIAL's appeal is still pending.

COUNT I

WARMUS' CLAIM FOR VIOLATION OF CIVIL RIGHTS

104. Plaintiff, WARMUS, realleges and reavers paragraphs 1 through 103 and said allegations are hereby incorporated herein as if the same were set forth fully herein.

105. WARMUS has been in the business of selling credit life and disability policies sold in connection with the financing of automobiles for over thirty years and developed a good relationship and outstanding reputation with numerous automobile dealers mostly located in Michigan whose agencies sold these policies of insurance to their customers.

106. Based upon the relationships and his reputation, WARMUS either individually or through companies which he controlled had the ability to be able to place the business from his accounts with another insurer, so long as WARMUS was involved, as had been done several times in WARMUS' thirty plus year career.

107. In early 1992 the Michigan Insurance Bureau enlisted the aid of MELAHN, OETTING and others at the MDI to aid the Michigan Insurance Bureau in its vendetta

against WARMUS with the goal to drive WARMUS out of the insurance industry and destroy AMERICAN FINANCIAL and his reputation and his relationship with the various automobile dealers and their agencies.

108. The actions above mentioned taken by MELAHN, HOBBS and OETTING were designed to drive WARMUS out of the insurance business and to destroy WARMUS' reputation and relationship with the various automobile dealers and their agencies by creating circumstances in which it was impossible for WARMUS or his companies to comply, misleading and deceiving WARMUS in order that he is prevented from taking actions to rectify concerns of MDI, or otherwise acted so as to prevent WARMUS from properly operating a profitable business.

109. Moreover, had MELAHN, HOBBS and OETTING not lied to WARMUS and AMERICAN FINANCIAL regarding the reinsurance credits, the acceptability of the reinsurance treaty with NRG for the last quarter of 1992, and numerous other matters as stated herein, AMERICAN FINANCIAL and WARMUS could have exercised their rights of judicial review pursuant to the Missouri Insurance Code, to challenge the actions of Defendants. Thus, the actions of Defendants effectively deprived AMERICAN FINANCIAL of its right of access to the courts.

110. The actions complained of by WARMUS in this Complaint were done by MELAHN, HOBBS and OETTING under color of law and deprived WARMUS of his property without substantive and procedural due process.

111. The actions by HOBBS, OETTING and MELAHN were malicious and in bad faith.

112. As a direct and proximate and foreseeable result of HOBBS, MELAHN and OETTING's actions, WARMUS suffered damages including damage to his reputation, a loss of consulting fees and other revenues derived from his book of business as well as the loss of the valuable property right in said book of business and was otherwise damages.

113. As a result of Defendants' actions, WARMUS hired the services of the undersigned Counsel and is obligated to pay said Counsel a reasonable fee for their services.

WHEREFORE, WARMUS demands judgment against OETTING, HOBBS, and MELAHN for damages, costs and attorney's fees and such other relief as the court deems necessary and proper.

COUNT II

WARMUS' CLAIM FOR ABUSE OF PROCESS

114. Plaintiff, WARMUS, realleges and reavers paragraphs 1 through 103, and said allegations are hereby incorporated herein as if the same were set forth fully herein.

115. MELAHN's actions in placing AMERICAN FINANCIAL into administrative Supervision and then filing for a Seizure and for a Rehabilitation were not for the purpose of saving or correcting problems with AMERICAN FINANCIAL or any other proper purpose, but rather for the purpose of destroying AMERICAN

FINANCIAL, destroying WARMUS's reputation, making it impossible for WARMUS to continue in the insurance business, and otherwise damaging WARMUS and AMERICAN FINANCIAL.

116. The actions by MELAHN in filing for an Administrative Supervision, Seizure and Rehabilitation were malicious and done intentionally to cause the damages above-stated.

117. As a direct and proximate and foreseeable result of MELAHN's actions, WARMUS suffered damages, including damage to his reputation, loss of consulting fees or other revenues derived from his book of business, as well as the loss of property rights in said book of business, and was otherwise damaged.

WHEREFORE, WARMUS demands judgment against HOBBS MELAHN and OETTING for damages, costs and any such further relief this court deems appropriate.

COUNT III

BREACH OF FIDUCIARY DUTY

118. Plaintiff, WARMUS, realleges and reavers paragraphs 1 through 103 and said allegations are hereby incorporated herein as if the same were set forth fully herein.

119. HOBBS, MELAHN and OETTING owed a fiduciary duty to AMERICAN FINANCIAL and its owners to deal with the company in good faith and in an honest and forthright manner.

120. HOBBS actions and representations on his own behalf or on behalf of MELAHN and OETTING to AMERICAN FINANCIAL and to WARMUS above mentioned regarding the accounting methodology for the LLOYDS treaty, the acceptability of the treaty with NRG, the volume of acceptable premium writing, the financial condition of AMERICAN FINANCIAL, the consequences of not filing an audited financial, and other misrepresentations and actions were false and misleading when made.

121. HOBBS, MELAHN and OETTING knew that said representations and actions were false when made and that their representations and actions would lead AMERICAN FINANCIAL and WARMUS into a false sense of security by having complied with all instructions of HOBBS, and prevent AMERICAN FINANCIAL and WARMUS from taking actions necessary for their survival, which actions would have been easy to take, if only AMERICAN FINANCIAL or WARMUS had known such actions were desired by MDI.

122. The representations and actions by HOBBS, MELAHN and OETTING were material and made and performed for the purposes of deceiving AMERICAN FINANCIAL or WARMUS.

123. Due to the nature of the fiduciary relationship between HOBBS, MELAHN, OETTING, AMERICAN FINANCIAL and WARMUS, AMERICAN FINANCIAL and WARMUS had a right to rely on the actions and misrepresentations of HOBBS, MELAHN and OETTING.

124. AMERICAN FINANCIAL and WARMUS did rely on the misrepresentations and actions of HOBBS, MELAHN and OETTING.

125. HOBBS, MELAHN and OETTING's actions as above described constituted a breach of said fiduciary duty and were fraudulent.

126. As a direct and proximate and foreseeable result of MELAHN's actions, WARMUS suffered damages, including damage to his reputation, loss of consulting fees or other revenues derived from his book of business, as well as the loss of property rights in said book of business, and was otherwise damaged.

WHEREFORE, WARMUS demands judgment against HOBBS, MELAHN and OETTING for damages, costs and any such further relief this court deems appropriate.

COUNT IV

WARMUS'S CLAIM FOR PRIMA FACIA [sic] TORT

127. Plaintiff, WARMUS, realleges and reavers paragraphs 1 through 103 and said allegations are hereby incorporated herein as if the same were set forth fully herein.

128. The actions above-described by HOBBS, MELAHN and OETTING were intentional and unlawful and done maliciously with the sole intent to damage WARMUS and AMERICAN WAY.

129. There was no justification for HOBBS, MELAHN and OETTING's acts described above.

130. As a direct and proximate and foreseeable result of MELAHN's actions, WARMUS suffered damages, including damage to his reputation, loss of consulting fees or other revenues derived from his book of

business, as well as the loss of property rights in said book of business, and was otherwise damaged.

WHEREFORE, WARMUS demands judgment against HOBBS, MELAHN and OETTING for damages, costs, and any such further relief this court deems appropriate.

DEMAND FOR JURY TRIAL

Plaintiff, WARMUS, demands trial by jury on all issues so triable.

Respectfully submitted,

HAWKINS LAW OFFICE
P.O. Box 1497
Jefferson City, MO
65102-1497
(314) 635-3000

/s/ Robert L. Hawkins, III
ROBERT L. HAWKINS, III
MO BAR #28169

RASSNER, RASSNER,
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/s/ Alan Gold
ALAN C. GOLD
FL BAR #304875

IN THE CIRCUIT COURT OF COLE COUNTY
STATE OF MISSOURI

JAY ANGOFF, Director, Department of Insurance State of Missouri	)	
Plaintiff,	)	Case No. CV193-107CC
vs.	)	
AMERICAN FINANCIAL SECURITY LIFE INSURANCE COMPANY	)	
Defendant.	)	

MOTION FOR AUTHORITY TO FILE SUIT ON BEHALF OF DEFENDANT

COMES NOW, Defendant, AMERICAN FINANCIAL SECURITY LIFE INSURANCE COMPANY (AMERICAN FINANCIAL), by and through its undersigned counsel, and requests that this Honorable Court permit it to file suit against LEWIS MELAHN (MELAHM), former Director of Missouri Department of Insurance, JAMES OETTING (OETTING), former Chief Financial Examiner for the Missouri Department of Insurance, WILLIAM HOBBS (HOBBS), former Administrator [sic] Supervisor of AMERICAN FINANCIAL, and possibly other present and former employees of the Missouri Department of Insurance (MDI) and, in support thereof, states as follows:

1. During the administrative supervision of AMERICAN FINANCIAL, various employees and representatives of MDI including, without limitation, MELAHN, OETTING AND HOBBS, took action in conjunction and

in conspiracy with the Michigan Insurance Bureau which were detrimental to AMERICAN FINANCIAL; made misrepresentations of material facts to the detriment of AMERICAN FINANCIAL; misled and deceived AMERICAN FINANCIAL in matters which were detrimental to AMERICAN FINANCIAL; and intentionally acted in conspiracy with the Michigan Insurance Bureau to destroy the company. The findings of the Master which have been ratified by this Court, particularly in its finding of estoppel against the State in several key areas, as well as the testimony during trial indicate the serious nature and truthfulness of these allegations against MELAHN, OETTING and HOBBS.

2. The individuals above-mentioned, as well as possibly other current and former employees of MDI committed tremendous waste of AMERICAN FINANCIAL's assets to which both the individual and the official State's bond should be held accountable.

3. There is a viable claim against MELAHN, OETTING, HOBBS and perhaps others for violation of the company's civil rights under 42 USC, Section 1983, as well as numerous claims under State law.

4. It would be a severe conflict of interest for Director Angoff to pursue this action.

5. AMERICAN FINANCIAL has requested of Director Angoff, through his counsel, that authority be delegated to the officers and directors of AMERICAN FINANCIAL to pursue this claim on behalf of the company.

6. Plaintiff refuses to grant permission to pursue this claim.

7. Defendant believes that the claim is necessary and would be a substantial asset of the company if it is pursued and requests authority of the Court for AMERICAN FINANCIAL to pursue this matter.

SUPPORTING MEMORANDUM

The issue is whether the Circuit Court of Cole County, Missouri which is vested under §375.1166 RSMo, with statutory authority to supervise the rehabilitation, possesses implied or inherent authority to empower the directors or the officers of AMERICAN FINANCIAL to initiate a legal suit on behalf of AMERICAN FINANCIAL to bring the assets of the company's claim against MELAHN, HOBBS AMERICAN FINANCIAL and OETTING into the estate in rehabilitation.

The Missouri Insurance Code does not provide the answer to this question nor are there any cases in Missouri which provide guidance. This matter is unique in part, because of the obvious conflict in the Plaintiff pursuing a cause of action against his predecessor, former employees of MDI and a person whom he just named as Special Deputy Rehabilitator.

The Missouri Insurance Code provides for Court supervision of the Rehabilitation and provides in certain circumstances for the Directors oppose [sic] actions of the Rehabilitator or even request a termination of the Rehabilitator. See §375.1166.1, 375.1168.1, 375.1168.2 and

375.1174 RSMo. See also *People ex rel. Schacht v. Main Insurance Company,* 448 N.E. 2d 950 (Ill.App. 1983)

In order to determine what remedies are appropriate to the Circuit Court under the circumstances, it is appropriate to examine the relief afforded by the United States Bankruptcy Court in virtually identical situations. Non-insurance companies in financial difficulties will often seek relief in Bankruptcy Court under Chapter 11, which is analogous to a rehabilitation. These companies in bankruptcies are operated by the prior owners known as "debtors in possession" or "court-appointed trustees" subject to the supervision of the court, until such time as a plan of reorganization can be adopted, or reorganization is abandoned and the company is liquidated. Thus, a rehabilitation under the Insurance Code is similar to a reorganization under the Bankruptcy Act, and thus, many courts in various states when examining questions regarding rehabilitation look to the United States Bankruptcy Courts for similarities and guidance.

During the period the company is being operated under the supervision of the Bankruptcy Court, all assets of the debtor, including causes of action against other parties, become the property of the estate, and only the trustee or debtor-in-possession has authority to collect them. Moreover, the courts have held, where the pursuit of a cause in action would increase the value of the estate, the debtor or trustee is obligated to collect it. See *Louisiana World Exposition v. Federal Insurance Company,* 858 F.2d 233 (5th Cir. 1988).

Situations regularly arise in the bankruptcy context where shareholders or creditors believe that a company

in Chapter 11 has a valid claim against a third party, but the trustee or debtor-in-possession refuses to pursue it. Although there is not a statutory basis for action by the bankruptcy courts to provide a remedy to the creditors or shareholders in that situation, the courts have provided one through their inherent powers. If the stockholders or creditors believe that the refusal of the trustee is unjustifiable, they can petition the court for relief. Although the bankruptcy courts have the power to grant more drastic remedies, the preferred remedy is for the court to specifically authorize the petitioning creditor or shareholder to institute an action for the benefit of the company in rehabilitation. See *Epstein, Nickles and White, Bankruptcy §6-2 (1992); In re Maclosky, 66 Fed. Supp. 620 (D.N.J. 1946); In re: Evergreen Valley Resort, Inc. 27 B.R. 75 (D. Maine 1983); In re: E.F. Hutton Southwest Properties II, Ltd. 103 B.R. 808 (Bkrtcy, N.D. Texas 1989)*

The procedures and justification for the granting of such authorization are fully explained in *Unsecured Creditors Committee v. Noyes,* 779 F.2d 901 (2d Cir. 1985). The Court pointed out that the authority for the creditors or shareholders to institute such suits in the name of the trustee is not explicitly found in the Bankruptcy Code, but exists as an "implied but qualified" right. *Unsecured Creditors Committee v. Noyes,* 779 F.2d 901 (2d Cir. 1985).

The trial court must first determine whether the parties seeking relief presents "a colorable claim or claims for relief that on appropriate proof would support a recovery". *Unsecured Creditors Committee v. Noyes,* 779 F.2d 901 (2d Cir. 1985), *Id.* at 905. If it makes such a finding, the court is obligated to then determine whether the trustee's refusal to bring such suit was unjustified.

This determination requires the court to examine "on affidavit and other submission, by evidentiary hearing or otherwise" *id.* at 905, whether there is a sufficient likelihood of success or to justify the anticipated delay and expense to the bankruptcy estate. If it is likely that the suit will bring in more assets to the estate that [sic] it will cost to prosecute, the court will authorize the petitioning creditors or shareholders to sue on behalf of the company in rehabilitation.

Where the claim is beneficial but the trustee refuses to sue because of the conflict of interest, the refusal is unjustified as a matter of law. *Louisiana Work Exposition v. Federal Insurance Company, supra,* 858 F.2d 233 (5th Cir. 1988) at 253, f.n.20.

This Honorable Court has sufficient authority to follow the same procedure in the present case. It should first require WARMUS to provide that either he has demanded that the Rehabilitator sue MELAHN, HOBBS or OETTING or that such demands be futile. WARMUS must then demonstrate that a cause of action against these three individuals presents "a colorable claim for relief that would support a recovery". If it does, the refusal of the Rehabilitator to sue on the claim is unjustified unless the Rehabilitator can show that the anticipated delay and expense to the estate outweighs the likelihood of success. Unless such a showing can be shown, WARMUS should be authorized to file the suit on behalf of AMERICAN FINANCIAL.

WARMUS through counsel has requested authority to sue and said authority has been denied. (A copy of

said letters requesting the authority as well as the denial is attached hereto as Exhibit "A" and "B" respectively)

The Findings by the Special Master as well as the transcript clearly evidence a viable claim for relief, and a clear likelihood of a clear success on the merits.

WHEREFORE, AMERICAN FINANCIAL requests that this Honorable Court grant it permission to file suit on behalf of AMERICAN FINANCIAL against MELAHN, HOBBS and OETTING and possibly others.

Respectfully submitted,

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700 E. Capital Avenue
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(314) 635-3000

/s/ Robert L. Hawkins
Robert L. Hawkins, III Esquire
MO BAR #28169

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(305) 667-0475

/s/ Alan C. Gold
Alan C. Gold, Esquire
FL BAR #304875

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing Motion For Authority To File Suit On Behalf Of Defendant was Federal Expressed this 14th day of May, 1993, to Elisabeth R. Sauer, SWANSON, MIDGLEY, GANGWERE, CLARKE & KITCHIN, 922 Walnut Street, Kansas City, MO 65106-1848 and Mark W. Stahlhuth,

General Counsel, Missouri Department of Insurance, 301 West High Street, Jefferson City, Missouri 65101.

By: /s/ Alan C. Gold
ALAN C. GOLD

RASSNER, RASSNER, KRAMER AND GOLD, P.A.
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May 3, 1993

via Fax to: S16-S42-0013 & Regular Mail

Elisabeth R. Sauer, Esquire
SWANSON, MIDGLEY, GANGWERE,
CLARKE & KITCHIN
Commerce Trust Building
922 Walnut, Suite 1500
Kansas City, MO 64106

RE: American Financial Security Life Insurance Corporation (American Financial)

Dear Ms. Sauer:

The stockholders of American Financial believe that the company's civil rights have been violated by Lewis Melahn, James Oetting and William Hobbs. We believe that viable claims exist against these individuals, and probably others, based upon 42 USC 1983, as well as certain state claims.

It is *imperative* that the company pursue these actions for damages. It would be impractical for Mr. Angoff to oversee this litigation, especially since we anticipate that, based upon discovery, additional defendants would need to be added, some of which are currently employees at the Department of Insurance. We request that authority be delegated to the officers and directors of American Financial to pursue this action on behalf of the company.

It is requested that an immediate response be given.

Very truly yours,

/s/ Alan C. Gold
ALAN C. GOLD

ACG/pvh

THE LAW FIRM OF
SWANSON - MIDGLEY -
GANGWERE - CLARKE & KITCHIN

[Names and addresses omitted in printing]

May 4, 1993

VIA FACSIMILE

Alan C. Gold, Esq.
Rassner, Rassner, Kramer
& Gold, P.A.
7000 S.W. 62nd Ave.
Penthouse B
South Miami, FL 33143

Re: Angoff v. AFSLIC

Dear Mr. Gold:

The Rehabilitator does not agree to delegate authority to the former officers and directors of AFSLIC to pursue litigation on behalf of AFSLIC against Mr. Lewis Melahn, Mr. James Oetting and/or Mr. Hobbs.

Any action taken by the suspended officers and directors on behalf of the company would violate the injunction.

Very truly yours,

/s/ Elisabeth R. Sauer
Elisabeth R. Sauer

ERS:dkr

cc Mr. Jay Angoff
Mark W. Stahlhuth, Esq.
Mr. William R. Hobbs, II
Robert L. Hawkins, III, Esq.

Supreme Court, U.S.
FILED
MAY 13 1996
CLERK

No. 95-1251

In The
SUPREME COURT OF THE UNITED STATES
October Term, 1995

THOMAS A. WARMUS,

Petitioner,
v.
LEWIS MELAHN, JAMES OETTING,
and WILLIAM R. HOBBS, II,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Eighth Circuit

BRIEF IN OPPOSITION

JEREMIAH W. (JAY) NIXON
Attorney General

JOHN R. MUNICH
Deputy Attorney General for Litigation

BRUCE FARMER*
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Post Office Box 899
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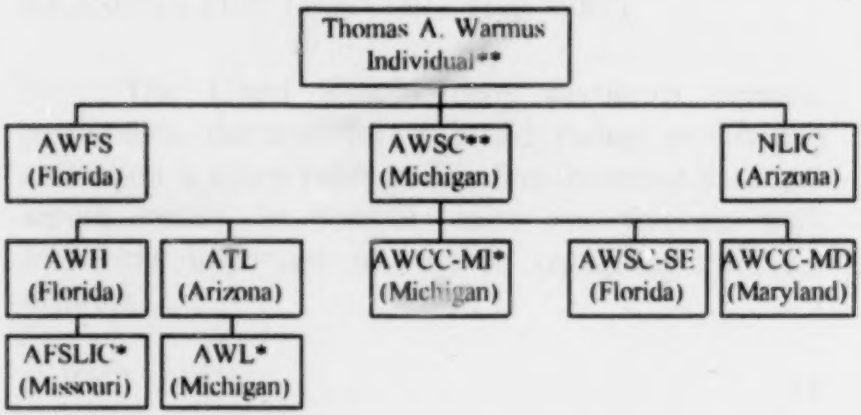
ATTORNEYS FOR RESPONDENTS
* Counsel of Record

LIST OF AFFILIATED COMPANIES

Petitioner Thomas Warmus is the owner of American Financial Life Insurance Company (AFSLIC). For purposes of this lawsuit, petitioner and this company are one and the same. AFSLIC is a member of an insurance holding company system as defined by Chapter 382.010, Mo.Rev.Stat. A Holding Company Registration Statement (HCRS) was filed on August 12, 1991 by AFSLIC for itself and all of its affiliates and subsidiaries. The following organizational chart depicts the holding company system of AFSLIC:



AWFS	American Way Financial Services Corporation
AWSC**	American Way Service Corporation
NLIC	Nanseekay Life Insurance Company
AWH	American Way Holdings, Incorporated
ATL	American Trend Life Insurance Company
AWCC-MI*	American Way Casualty Company of Michigan
AWSC-SE	American Way Service Corporation Southeast
AWCC-MD	American Way Casualty Company of Maryland
AFSLIC*	American Fin. Sec. Life Insurance Company
AWL*	American Way of Life Insurance Company

* Denotes company in Rehabilitation

** Denotes Chapter 11 Bankruptcy.

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RESPONDENTS' STATEMENT OF THE CASE

Having failed in the Missouri state courts four times, twice without an appeal, to derail a pending insurance regulatory proceeding against his company, petitioner now seeks review of a particularly fact-sensitive ruling of the lower federal courts in an area of law -- insurance regulation -- peculiarly committed to the province of the states. The decision of which he seeks review is fully consistent with past abstention decisions of this Court. Indeed, the issues raised in the petition are presently governed by well-established law. The position petitioner urges would, in fact, radically change that well-established law and place ongoing state insurance proceedings at the mercy of every affected party who could afford a federal court filing fee.

To the extent petitioner seeks to pose discrete, carefully drawn issues to evade the established abstention principles, those issues are almost totally devoid of any development among the courts of appeals. At bottom, petitioner is left to argue only that the Eighth Circuit erred in ruling he could not disrupt complex, ongoing state insurance proceedings through the vehicle of the Section 1983 damages action he filed in federal court. But even if that ruling were wrong -- and it is not -- the petition would still present no issues worthy of review by this Court. Indeed, granting the petition would yield precisely the result petitioner seeks -- disruption of the ongoing State regulatory proceedings. The petition should be denied.

Facts

The record and legal basis for the lower court decisions have not been accurately presented in petitioner's argument for certiorari. Because of the unique factual background relating to petitioner and his various corporations, it is important to correct petitioner's misrepresentations. Additionally, subsequent events, including pending criminal charges and bankruptcy proceedings involving petitioner, warrant consideration in deciding whether to grant the petition.

In early 1992, Lewis Melahn, the former Director of the Missouri Department of Insurance (MDI), placed American Financial Security Life Insurance Company (AFSLIC) into administrative supervision pursuant to Missouri's comprehensive statutory scheme to regulate financially-distressed insurance companies. Mo. Rev. Stat. §§ 375.1150 - 375.1246 (1994). William R. Hobbs, II, was appointed and acted as the administrative supervisor of AFSLIC. Acting on a verified petition, the state court issued an order of rehabilitation, finding that MDI officials had "proved grounds sufficient to place . . . AFSLIC into rehabilitation pursuant to Section 375.1165, R.S.Mo. because AFSLIC is operating in hazardous condition." App. at 62. The rehabilitation court adopted as its findings of fact and conclusions of law the special master's report. The report found, as grounds for an order authorizing rehabilitation, that the further transaction of business by AFSLIC was hazardous to its policyholders, creditors, or the public under Mo. Rev. Stat. § 375.1165(1). App. at 55, 57. The report

specifically found: 1) AFSLIC's ratio of written premiums to capital and surplus was excessive, 2) AFSLIC overstated its reserve credits and resulting surplus, and 3) AFSLIC's admissible assets were less than its liabilities plus capital and surplus. *Id.*[1] It was Melahn's verified petition for rehabilitation, filed in his capacity as Director of MDI, that led to the order of rehabilitation.

On March 30, 1993, the Circuit Court of Cole County, Missouri, entered an order of rehabilitation, authorizing Jay Angoff, the present Director of MDI, to rehabilitate AFSLIC. App. at 61-64. The director, as rehabilitator, was authorized to appoint one or more special deputies who were granted the power and responsibility of the rehabilitator. The director appointed Hobbs as Special Deputy Rehabilitator.

Warmus and AFSLIC moved in the Missouri trial court for authority to file suit against Melahn, Hobbs, and James Oetting, former Chief Financial Examiner of the Department of Insurance. App. at 97. Warmus and AFSLIC moved to sue respondents individually for their actions "[d]uring the administrative supervision of" AFSLIC that subsequently led to the placement of AFSLIC into

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[1]The state petition for rehabilitation identified eight separate reasons for placing AFSLIC in rehabilitation. App. at 20. Only one ground was necessary to uphold the rehabilitation. And the state court held that rehabilitation was appropriate for three different reasons.

rehabilitation. *Id.* On June 10, 1993, the Missouri trial court denied Warmus and AFSLIC's motion. Neither Warmus nor AFSLIC ever appealed that denial to the Missouri appellate court.

AFSLIC appealed the order of rehabilitation in the Missouri courts. The Missouri appellate court affirmed the order of rehabilitation, holding that "there was substantial evidence from which the trial court could find AFSLIC should have been placed into rehabilitation." *Angoff v. American Fin. Sec. Life Ins. Co.*, 869 S.W.2d 90, 93 (Mo. Ct. App. 1993) (*Angoff I*). The court stated:

> The Director sought rehabilitation for AFSLIC for operating with excessive premiums to assets, overstating its reserve credits, and for failing to maintain the required amount of capital and surplus. The trial court found all of these things to be true to some extent and additionally found the accounting methodology that AFSLIC used evidenced hazardous operating conditions.

Id. at 93. The Missouri appellate court upheld the validity of the respondents' actions in placing AFSLIC into rehabilitation.[2]

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[2]The Missouri appeal was initially decided on November 9, 1993. The district court's opinion dismissing the federal court lawsuit was issued on November 29, 1993. The Missouri decision became

The state court rehabilitation proceeding continues.[3] Warmus has filed numerous motions in the rehabilitation court, including three motions to terminate the rehabilitation.[4] The first motion to terminate was filed August 17, 1993. Summary judgment was entered against Warmus on December 21, 1993 and Warmus did not appeal. The second motion was filed December 21, 1993. After opening statements, the trial court directed a verdict against Warmus. Warmus appealed, but the Missouri appellate court affirmed the denial of his motion to terminate. *Angoff v. American Fin. Sec. Life Ins. Co.*, 891 S.W.2d 833 (Mo. Ct. App. 1994) (*Angoff II*). Warmus' third motion to terminate was denied by the trial court and again Warmus did not appeal. Warmus, as representative of the suspended directors of AFSLIC, has also filed a motion for money damages against the

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final on February 22, 1994 when the Missouri Supreme Court denied AFSLIC's application for transfer. App. 18.

[3]Under separate cover, respondents have submitted various court records and documents from other litigation involving Warmus including 1) the ongoing state rehabilitation case, 2) Warmus' individual bankruptcy, 3) Warmus' holding company bankruptcy and 4) pending criminal charges against Warmus.

[4]On July 6, 1993, the suspended officers and directors of AFSLIC filed a Designation of Representative, designating Warmus as their corporate representative for all purposes in the AFSLIC rehabilitation.

Missouri Department of Insurance.[5] This motion is pending in state court.

Though Warmus states that he "was never party to the state court rehabilitation proceedings of AFSLIC," Pet. at 3, he does not seriously challenge the Eighth Circuit's finding that Warmus and AFSLIC are "one and the same" for abstention purposes. *Warmus v. Melahn*, 62 F.3d 252, 257 (8th Cir. 1995); App. at 11. There are two pending bankruptcy cases involving Warmus that support this finding. Warmus has filed an individual Chapter 11 bankruptcy in the United States Bankruptcy Court, Southern District of Florida. *In re: Warmus*, Case No. 94-24673-BKC-RBR. There Warmus includes the instant lawsuit in the Notice of Filing Schedules and Statement of Affairs. The second bankruptcy involves Warmus' holding company. In this Chapter 11 bankruptcy, the statement of financial affairs again lists this federal lawsuit. *In re: American Way Service Corp.*, Case No. 94-24696-BKC-RBR.

Finally, the underlying federal lawsuit alleges that Missouri insurance officials conspired with officials of the Michigan Insurance Bureau. Pet. at 2. The Court should be aware that the state of Michigan has charged Warmus with six felonies related to his control of two insurance firms. *People v. Warmus*, Case No. CR95-137002 FH (Circuit Court of Oakland County, Michigan). Warmus has also filed at least one

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[5]Motion to Assess Missouri Division [sic] of Insurance for Waste and Extraordinary Expenses filed on September 13, 1994 in the state rehabilitation court.

federal action against Michigan insurance officials. *Warmus v. Hank*, 48 F.3d 1220 (6th Cir. 1995) (unpublished).

REASONS FOR DENYING THE WRIT

The Court should deny certiorari because petitioner's demand for a broad ruling prohibiting abstention is unworkable in this fact-intensive case and would result in federal court interference with Missouri's important interest in regulating insolvent insurers.

Warmus presents abstention issues under a broad analytical framework. The abstention doctrines, however, are not easily reduced to bright-line resolution. The complex interplay between the federal and state systems, so integral to our system of federalism, requires careful consideration of the factual and legal issues involved in each case. Therefore, it is not surprising that this Court has yet to decide the extent to which the *Younger* doctrine applies to a federal action seeking only monetary relief. And it should not do so in a case that presents unique factual issues in an area expressly left for the states to regulate.

1. Petitioner misrepresents the fact-intensive nature of this case.

Petitioner's conclusory presentation of the facts is perhaps most disturbing. Warmus glosses over important facts and distorts those he chooses to present. For example, Warmus argues that the state court proceedings and the federal case "were completely

different." Pet. 8. But even a cursory review of the federal complaint shows the substantial, indeed, almost identical, relationship between Warmus' claim for money damages and the state court rehabilitation proceeding for AFSLIC. The federal complaint refers to Warmus and AFSLIC interchangeably. App. 66-96. In fact, the federal complaint specifically alleges that respondent Melahn's "actions in placing [AFSLIC] into administrative supervision and then filing for a Seizure and for a Rehabilitation were . . . for the purpose of destroying . . . and otherwise damaging Warmus and [AFSLIC]." App. at 92-93.

Warmus states that he did not contest the validity of the order placing AFSLIC into rehabilitation. Pet. at 2-3. The record shows otherwise. In state court, Warmus has appealed the rehabilitation proceeding twice. First, Warmus appealed the initial order of rehabilitation challenging the actions of state officials. His first appeal was rejected. *Angoff I*, 869 S.W.2d at 93. Warmus also appealed the second of three motions to terminate the rehabilitation proceeding. Again, the Missouri appellate court rejected Warmus' challenge, finding that AFSLIC remained insolvent and in an hazardous condition. *Angoff II*, 891 S.W.2d at 835. Thus, the state court of appeals has twice determined that the rehabilitation proceeding was lawful.

Now, in federal court, Warmus is mounting a direct attack against the state court judgment placing AFSLIC into rehabilitation. Warmus calculates his money damages based upon the respondents' actions in placing AFSLIC under administrative supervision and

requesting a rehabilitation order. Warmus' claim for monetary damages against the individual state officials is inextricably linked with respondents' official decisions to place AFSLIC into a state court rehabilitation proceeding. A federal court damage action would provide Warmus with yet another opportunity to challenge the conduct of state officials that resulted in AFSLIC's rehabilitation proceeding, conduct that has already been validated by the state appellate court.[6]

An accurate review of the factual record reveals the uniqueness and complexity of this case. While lawsuits involving insolvent insurers are not uncommon, the instant petition is factually distinct from even that type of litigation. For example, the Eighth Circuit identified three major categories of cases involving insurer insolvency abstention issues. *Wolfson v. Mutual Benefit Life Ins. Co.*, 51 F.3d 141, 145 (8th Cir. 1995). The first category consisted of suits by the insolvent insurer's policyholders against third parties in which the defendant, often supported by the insurer's receiver, urges abstention because recovery by the plaintiff may reduce the receiver's ability to recover on

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[6]To illustrate, Warmus seeks damages in federal court for loss of consulting fees, other revenue and "loss of property rights" in his "book of business." App. at 92. These are in fact assets of AFSLIC which the state court has ordered the rehabilitator to collect. It would directly conflict with the state court rehabilitation order if a federal court ordered payment to Warmus.

behalf of the insurer's insolvency estate. The second category involved cases in which the insolvent insurer or its receiver asserted a claim in the federal action which, if successful, will enhance the insolvent's estate. The third category identified by the Eighth Circuit involved claims by policyholders, policy beneficiaries, and other creditors against a now-insolvent insurer.

Warmus' petition does not fit within any of these categories, but presents a wholly different, and rare (at least in the caselaw) scenario.[7] Warmus' federal lawsuit pits an insolvent insurer against the state officials who, as twice validated by the state court, properly found the insurance company to be financially insolvent and properly placed the company into rehabilitation. A broad abstention ruling under the unique facts of this case would have little precedential value and offer little guidance to the lower courts.

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[7]This case is also different from *Quackenbush v. Allstate Ins. Co.*, No. 95-244 (U.S. argued Feb. 20, 1996), awaiting decision by this Court. *Quackenbush* involves two issues: 1) the appealability of a remand order based on abstention and 2) the application of *Burford* abstention to actions in equity. There, Allstate seeks to arbitrate its dispute with the liquidator of an insolvent insurer pursuant to reinsurance contracts between Allstate and the insurer. Allstate, unlike Warmus, does not seek damages against the state officials.

2. Petitioner misrepresents the Eighth Circuit's holding, which is premised on established legal principles.

Contrary to petitioner's statement, the Eighth Circuit did not hold that a finding in Warmus' favor could cause "embarrassment to the MDI." Pet. at 7. The Eighth Circuit actually held that a finding in Warmus' favor "might well have the practical effect of undermining the validity and integrity of the state-court rehabilitation proceedings." App. at 9. The court first noted that the respondents' "conduct was clearly in issue in AFSLIC's appeal." *Id.* The court also found that a "resulting federal judgment" for damages would amount to a declaration that high ranking officials at MDI conspired to drive Warmus out of business. *Id.* Relying on this court's opinion in *Samuels v. Mackell*, 401 U.S. 66 (1971), the Eighth Circuit recognized that Warmus' federal lawsuit for money damages could have a substantial impact on or interfere with AFSLIC's state court rehabilitation proceeding. Whether the federal court lawsuit requests damages or equitable relief, the practical effect is virtually identical. The pending state court proceeding could be frustrated as much by a damage award as it would be by an injunction.

"The potential for federal-state friction is obvious." *Deakins v. Monaghan*, 484 U.S. 193, 208 (1988) (J. White concurring) (citation omitted). Application of comity principles allow federal courts to avoid this friction. This Court has already recognized that abstention is appropriate in § 1983 damage actions where to do so would be intrusive to state interests. In

Fair Assessment in Real Estate Ass'n, Inc. v. McNary, 454 U.S. 100 (1981), state taxpayers brought suit for damages in federal court alleging the unconstitutional administration of the state tax system. There, the taxpayers, like Warmus, claimed that damage actions were inherently less intrusive to state interests than injunctions or declaratory judgments and therefore should not be barred from federal court. There, the taxpayers, like Warmus, argued that they only sought recovery from individual state officers. 454 U.S. at 113. The Court held that "a determination [in a damage action] would be fully as intrusive as the equitable actions that are barred by principles of comity." *Id.* (footnote omitted). The Court also emphasized that "the intrusiveness of such § 1983 actions would be exacerbated by the nonexhaustion doctrine of *Monroe v. Pape*, 365 U.S. 167, 81 S.Ct. 473, 51 L.Ed.2d 492 (1961)." *Id.* at 113-14.

And while a judgment alone is intrusive, "the very maintenance of the suit itself would intrude on the enforcement of the state scheme." *Fair Assessment in Real Estate*, 454 U.S. at 114. Warmus' view would mandate federal court intrusion into the entire scope of the state regulatory authority over financially-distressed insurers, from supervision to rehabilitation to liquidation. An individual, like Warmus, could attack every regulatory decision in a federal § 1983 action for damages.[8] "[D]amages actions, no less than actions for

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[8]For example, in state court, Warmus has filed three motions to terminate the rehabilitation, a motion to assess damages and numerous other motions objecting

an injunction, would hale state officers into federal court every time a [plaintiff] alleged the requisite elements of a § 1983 claim." *Id.* at 115. State officials' determination, and even authority, to regulate would be drained.

Warmus also suggests that when he chooses to mount a federal court attack on a state regulatory action, the federal court must apply a harsh and unprecedented standard. Plucking the word "substantial" from this Court's abstention jurisprudence,[9] Warmus radically narrows *Younger* abstention to cases in which a party can demonstrate "substantial interference" with a certain state proceeding. This Court has routinely rejected this approach, noting that "the substantiality of [a] State's interest in its proceedings" is not examined by narrowly inquiring into "its interest in the *outcome* of the particular case." *New Orleans Pub. Serv., Inc. v. Council of City of New Orleans*, 491 U.S. 350, 365 (1989) (emphasis in original) (*NOPSI*). Such an interest could arguably -- and simply -- "be offset by a substantial federal interest in the opposite outcome." *Id.* Instead, focus is placed on "the importance of the generic proceedings to the State." *Id.*

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to routine regulatory decisions. Under Warmus' view of abstention, he can seek federal court review of these disputes simply by limiting his prayer to money damages.

[9]Pet. at 11, citing *Middlesex County Ethics Comm. v. Garden State Bar Ass'n*, 457 U.S. 423, 432 (1982).

Thus, for example, in *Younger v. Harris* the Court focused on California's generic interest in carrying out the task of enforcing its criminal laws. 401 U.S. 37, 51-52 (1971). In *Ohio Civil Rights Comm'n v. Dayton Christian Schools, Inc.*, another case in which the Court approved of abstention, the focus was placed on Ohio's general interest in preventing employers from engaging in sexual discrimination. 477 U.S. 619, 628 (1986). In *Middlesex County Ethics Comm.*, 457 U.S. at 434, the Court focused on New Jersey's "important interest in maintaining and assuring the professional conduct of the attorneys it licenses." These cases recognize that abstention is particularly appropriate where a specialized state proceeding exists and the federal inquiry would likely frustrate or undermine the state action.

Warmus does not dispute Missouri's legitimate interest in regulating its insurance industry. Missouri has a comprehensive scheme to regulate financially-impaired insurance companies. Mo. Rev. Stat. §§ 375.1150 - 375.1246. And Congress has statutorily recognized the "supremacy of the States in the realm of insurance regulation" by passing the McCarran-Ferguson Act, 15 U.S.C. §§ 1011-1015. *U.S. Dep't of Treasury v. Fabe*, 508 U.S. 491 (1993).

The underlying action is intimately connected with a state statutory scheme and the operation of a highly regulated industry long recognized as involving vital public concerns. The Eighth Circuit's holding in this factually unusual case recognizes that *Younger* abstention permits the states to operate in their spheres of interest without unnecessary federal interference.

This holding is correct and does not warrant further review.

3. Abstention cannot be decided solely on the basis of the relief requested.

This Court has rejected Warmus' underlying premise, that abstention is susceptible to bright-line rules.

> [T]he decision whether to dismiss a federal action because of parallel state-court litigation does not rest on a mechanical checklist, but on a careful balancing of the important factors as they apply in a given case . . ..

Moses H. Cone Memorial Hosp. v. Mercury Constr. Corp., 460 U.S. 1, 16 (1983). The Court noted that the "weight to be given to any one factor may vary greatly from case to case, depending on the particular setting of the case." *Id.* The particular setting of this case, insurance regulation, is an area of state concern and, thus, is a significant factor in favor of both granting abstention and denying certiorari.

"The various types of abstention are," obviously, "not rigid pigeonholes into which federal courts must try to fit cases," *NOPSI*, 491 U.S. at 359 (citation omitted), any more than such cases may be pigeonholed simply by asking what type of relief a plaintiff determined to request. To the contrary, the abstention "fit" of a particular case is not dependent upon the type of relief requested. *Steffel v. Thompson*,

415 U.S. 452, 474-75 (1974); *Lake Carriers' Ass'n v. MacMullan*, 406 U.S. 498, 509 n.13 (1972); *Zwickler v. Koota*, 389 U.S. 241, 254 (1967). This Court should not adopt a rule whereby an artifice of pleading allows a party to avoid abstention and eliminates the courts' discretionary power.

Warmus' pleading-based view of abstention is only supported by the Fifth Circuit. *See, e.g., Alexander v. Ieyoub*, 62 F.3d 709, 713 (5th Cir. 1995) (*Younger* has no applicability to a claim for damages). Considering the factual posture of this case and the lack of a significant split in the circuits, the Court should defer consideration of this issue.

Moreover, this Court has approved federal court abstention in a variety of cases seeking legal remedies: RICO claims, *Tafflin v. Levitt*, 493 U.S. 455 (1990); a tax case for damages under § 1983, *Fair Assessment in Real Estate Ass'n*, 454 U.S. 100; a diversity suit for contractual reimbursement, *United Gas Pipe Line Co. v. Ideal Cement Co.*, 369 U.S. 134 (1962); a diversity suit concerning an action on an insurance policy, *Clay v. Sun Ins. Office Ltd.*, 363 U.S. 207 (1960); an eminent domain suit, *Louisiana Power & Light Co. v. City of Thibodaux*, 360 U.S. 25 (1959); a diversity suit for property damage dismissed on the basis of *forum non conveniens*, *Gulf Oil Corp. v. Gilbert*, 330 U.S. 501 (1947); an admiralty claim, *Langnes v. Green*, 282 U.S. 531 (1931); and others. Here, the lower courts' abstention simply reflect this well-established caselaw -- caselaw that examines the facts and the nature of the states' interests.

Abstention is a fact-specific inquiry. *Moses H. Cone*, 460 U.S. at 16. Abstention also requires the exercise of a federal court's discretionary power. *Younger v. Harris*, 401 U.S. 37, 43-44 (1971) (decision to abstain rests on principles of "equity" and considerations of "comity"). Indeed, the standard of review for a grant or denial of abstention is an abuse of discretion. *Moses H. Cone*, 460 U.S. at 19. But Warmus' litmus test would place abstention doctrines into watertight compartments and largely eliminate the ability of a federal judge to exercise his or her discretionary power. To forbid even the possibility of abstention in a case "at law" would unreasonably curtail the ability of the judiciary to perform one of its important functions: the striking of a reasoned balance between state and federal interests. Warmus' litmus test summarily casts aside this Court's decades-long development of a sensitive scale that delicately balances state and federal interests.

Finally, Warmus suggests the lower courts made a mistake in dismissing, rather than staying, his action for damages. Mistake is not a basis for certiorari. Further, a dismissal, rather than a stay, was appropriate because Warmus chose to abandon the claim for money damages he asserted in the state court proceeding. Because of that fact alone, Warmus' reliance on *Deakins v. Monaghan*, 484 U.S. 193, is misplaced. In *Deakins*, this Court held that the district court had "no discretion to dismiss rather than to stay claims for monetary relief that [could] not be redressed in the state proceeding." 484 U.S. at 202. And this Court has refused to allow a party to avoid *Younger* abstention by abandoning state appellate remedies.

Huffman v. Pursue, Ltd., 420 U.S. 592, 609 (1975); *see also NOPSI*, 491 U.S. at 369 ("a party may not procure federal intervention by terminating the state judicial process prematurely -- foregoing the state appeal to attack the trial court's judgment in federal court").

In this case, petitioner abandoned his state court remedies in order to demand that a federal court intrude upon a state's ability and right to rehabilitate an insolvent insurance company. Not surprisingly, petitioner demands that this Court impose a wholly unnecessary and unwise rule, one that would work to his benefit. To reduce abstention to a bright-line rule or litmus test and remove federal judges' discretion to abstain in money damages cases would curtail the ability of the judiciary to strike a balance between state and federal interests.

CONCLUSION

For the reasons stated above, the petition for writ of certiorari should be denied.

Respectfully submitted,

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